Supreme Court, U. S.
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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1978

No. 78-1207

NORMAN B. FROST, Deceased,
and
HARRY DREISEN,

Petitioners,

v.

EXECUTORS OF THE ESTATE OF ARTHUR R. MORRISON,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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No.

NORMAN B. FROST, Deceased,
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HARRY DREISEN,

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v.

EXECUTORS OF THE ESTATE OF ARTHUR R. MORRISON,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioners Norman B. Frost, deceased, and Harry Dreisen respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fourth Circuit entered in this proceeding on September 29, 1978.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit (App. A at 1a) entered on September

29, 1978 is reported at 584 F.2d 652. The opinion of the District Court (App. E at 41a) entered on February 3, 1975 is unreported.

JURISDICTION

The judgment of the Fourth Circuit was entered on September 29, 1978. A timely petition for rehearing *en banc* was denied on November 9, 1978, and this petition for certiorari was filed within 90 days of that date. The Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

QUESTIONS PRESENTED

1. Whether it is constitutionally permissible to apply the doctrine of "law of the case" to nonparties.

2. Whether it is constitutionally permissible to use the doctrine of "law of the case" to require newly joined parties to present new evidence in order to gain reversal of a decision adjudicating their rights made when they were not parties.

CONSTITUTIONAL PROVISION INVOLVED

The Fifth Amendment to the United States Constitution provides in pertinent part:

> No person shall . . . be deprived of life, liberty or property without due process of law . . . .

STATEMENT OF THE CASE

The Estate of Arthur R. Morrison (Morrison Estate) made a claim in the District Court that it was the beneficial owner under a constructive trust of two promissory notes. The notes were made by Do-Mor, Inc. in 1963 and were secured by a mortgage to land in Brevard County, Florida.[1] In an opinion dated May 4, 1971, the District Court imposed a constructive trust on the Brevard County, Florida land in favor of the Morrison Estate against Capital Investors, Co. (Capital). App. I at 109a-16a.

The Morrison Estate learned that in 1965 Capital had sold the notes to Norman B. Frost. Frost sold Harry Dreisen an interest in the notes. The Morrison Estate attempted to impose the May 1971 constructive trust against Frost and Dreisen, the true owners of the notes and Florida land.[2] As a result of action by the Morrison Estate, Frost and Dreisen were added as parties to the case by an order of the District Court dated December 16, 1971. App. H at 98a. Frost and Dreisen were added as parties *after* the District Court's May 1971 imposition of the constructive trust in favor of the Morrison Estate against Capital.

In an opinion dated August 25, 1972, the District Court ruled that it would *not* impose a constructive trust in favor of the Morrison Estate against Frost and Dreisen. App. G at 78a. The District Court observed that it had not intended to bind persons who were not parties to the case by its May 1971 ruling imposing a constructive trust against Capital. App. G at 89a-90a. The District Court, after a hearing at which Frost and

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[1] The Morrison Estate's claim to a constructive trust was made in a diversity case involving many parties and issues not relevant to this petition. Opinions in the case not relevant to the petition are reported at 453 F.2d 1364 (4th Cir. 1972); 387 F.2d 591 (4th Cir. 1967), 360 F.2d 462 (4th Cir. 1966).

[2] The notes were in default. Frost and Dreisen foreclosed on the mortgage. At foreclosure, the Florida land was sold at public auction to the Estate of Frost, Frost having died, and Dreisen. App. A at 16a n.6; App. E at 45a.

Dreisen were present as parties, ruled that a review of all of the evidence supported a conclusion substantially different from that expressed by the District Court in its May 1971 opinion. App. G at 78a.

The Morrison Estate appealed the District Court's August 1972 ruling refusing to impose the May 1971 constructive trust against Frost and Dreisen. In an opinion dated September 12, 1973, the Fourth Circuit reversed and remanded the case with directions. The reversal was based upon the District Court's failure to apply applicable principles of the Uniform Commercial Code to the determination of whether to impose the constructive trust against Frost and Dreisen. The Fourth Circuit's remand instructions were:

> The issue of a constructive trust in the notes in favor of the estate accordingly remains for resolution between the estate and the defendants Frost and Dreisen. The cause is remanded to the District Court to make appropriate findings on that issue on the record heretofore made before it, supplemented by any additional evidence either party may submit.

App. F at 72a; reported at 484 F.2d 1157, 1163 (4th Cir. 1973).

In another part of its opinion of September 1973, the Fourth Circuit found that Frost and Dreisen were *not* in privity with Capital. The court stated that, although in its May 1971 opinion the District Court had found that the Morrison Estate was entitled to a constructive trust in the notes or their proceeds, the District Court had expressly reserved judgment on the rights of Frost and Dreisen. The Fourth Circuit ruled that,

> [I]t would seem entirely improper to apply to Frost and Dreisen any mechanical rule of privity

> so as to bar them from a right to be heard on the existence *vel non* of a constructive trust in favor of the estate in and to the notes . . . . On the basis of the 'circumstances' of this case, the application of the principle [of privity], in our opinion, would not accord with fundamental fairness.

App. F at 71a-72a.

On remand, in an opinion dated February 3, 1975, the District Court applied Uniform Commercial Code principles and *again refused* to apply the May 1971 constructive trust against Frost and Dreisen. App. E at 41a. The Morrison Estate appealed the District Court's February 3, 1975 decision.

In a unanimous opinion dated November 24, 1976, the Fourth Circuit affirmed the District Court's February 1975 refusal to apply the constructive trust to Frost and Dreisen.[3] App. D at 31a. The Morrison Estate filed a Petition for Rehearing and Request for Rehearing *En Banc*. Without permitting Frost and Dreisen an opportunity to reply,[4] the Fourth Circuit panel, with Circuit Judge Widener dissenting, entered an opinion dated March 4, 1977, reversing the District Court and entering judgment against Frost and Dreisen. App. C at 26a. Frost and Dreisen filed a Petition for Rehearing and Request for Rehearing *En Banc*. By an order filed March 29, 1977, the Fourth Circuit withdrew its opinions of November 24, 1976 and March 4, 1977 and admitted that it had

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[3] The opinion was published in the advance sheets at 545 F.2d 877. However, the opinion was withdrawn from the bound volume at the request of the court. See the Editor's note at 545 F.2d 877.

[4] *See* Rule 40(a), Federal Rules of Appellate Procedure.

"acted improvidently" in entering its opinion of March 4, 1977. App. B at 24a. The court ordered additional briefs and argument.

On September 29, 1978, the Fourth Circuit entered an opinion, with Circuit Judge Widener dissenting, reversing the District Court's February 3, 1975 decision. The court held that the doctrine of "law of the case" required the District Court to adhere to its May 1971 decision imposing a constructive trust and to apply the decision to *nonparties* Frost and Dreisen. App. A at 4a. The court did not dispute the fact that Frost and Dreisen were not parties to the case at the time of the May 1971 District Court decision, but found that Frost and Dreisen had presented no new evidentiary basis to support the District Court's refusal to apply the constructive trust against them. App. A at 4a.

In the vigorous dissent, it was stated that application of the doctrine of "law of the case" to nonparties, nonprivies, violated fundamental constitutional principles guarantying Frost and Dreisen the right to be present in the case when judgment was entered against them. In commenting on the Fourth Circuit's requirement that Frost and Dreisen present new evidence to overcome a ruling made when they were not parties to the case, the dissenting Circuit Judge stated: "I think the rule the court today announces of requiring a new evidentiary basis for a new party, rather than a reconsideration of the evidence in the light of the fact that there are new parties, does not withstand either logical or constitutional analysis." App. A at 12a. The majority opinion did not address the constitutional reasoning advanced by the dissent.

REASONS FOR GRANTING THE WRIT

I.

THE DECISION BELOW RAISES SIGNIFICANT QUESTIONS CONCERNING THE CONSTITUTIONALITY OF APPLYING THE DOCTRINE OF LAW OF THE CASE TO NONPARTIES

In determining the rights of Frost and Dreisen, the Fourth Circuit relied upon a decision made in the District Court prior to the time Frost and Dreisen were joined as parties. The court justified its holding by claiming that "the principles of law of the case required adherence" to the earlier findings. App. A at 4a. The application of the doctrine of "law of the case" to bind nonparties presents a serious threat to fundamental tenets of constitutional Due Process.

A basic principle of Anglo-American jurisprudence is that nonparties may not be bound by an *in personam* adjudication. *Provident Tradesmen's Bank & Trust Co. v. Patterson*, 390 U.S. 102, 110 (1968); *Hansberry v. Lee*, 311 U.S. 32, 40-41, 45 (1940); *Pennoyer v. Neff*, 95 U.S. 714, 730-31, 733-34 (1878). Although the principle is not absolute, its exceptions have been narrowly drawn. This Court has not yet addressed the constitutional issues raised by the adjudication of the rights of nonparties by application of the doctrine of "law of the case." Cases which discuss the application of collateral estoppel or *res judicata* to nonparties provide examples of this Court's serious concern with the constitutional dimensions of the issue. *Parklane Hosiery Co. v. Shore*, 47 U.S.L.W. 4079 (January 9, 1979), is a recent example of the Court's concern for the rights of nonparties in the context of collateral estoppel. *See also Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*,

402 U.S. 313, 329 (1971). The present case embodies a dangerous and unconstitutional expansion of the concept of the "offensive use" of estoppel principles.

The Fourth Circuit, in the opinion below, states that "law of the case" permits, and even *requires*, courts to preclude re-litigation of prior decisions by newly joined parties.[5] The cases cited above show that the Fourth Circuit's decision is at odds with the constitutional interpretations which this Court has expressed in similar areas of the law.

"Law of the case" is a judicially created "rule of practice, based upon sound policy that when an issue is once litigated and decided that should be the end of the matter." *United States v. United States Smelting, Refining and Mining Co.*, 339 U.S. 186, 198 (1950). Unlike doctrines such as *res judicata*, which compel a court to defer to earlier judgments, "law of the case" is directed to a court's discretion and good sense. *Southern Ry. v. Clift*, 260 U.S. 316, 319 (1922); *Higgins v. California Prune & Apricot Grower, Inc.*, 3 F.2d 896, 898 (2d Cir. 1924) (Per Hand, J.). The opinion below effectively rejects the discretionary aspects of "law of the case" and states that the doctrine *requires* adherence to the prior decision. App. A at 4a.

The application of "law of the case" is generally restricted to persons who were parties to the case at the

[5]The Fourth Circuit's reliance upon "law of the case" to adjudicate the rights of nonparties Frost and Dreisen in the instant case deviates from the same court's concern for the rights of nonparties in other contexts. *E.g.*, *Edmonds v. Compagnie General Transatlantique*, 577 F.2d 1153, 1156 (4th Cir. 1978) (refusal to adjudicate the rights of nonparty stevedore).

time of the earlier decision. *See, e.g., Steinman v. Clinchfield Coal Corp.*, 121 Va. 611, 620-23, 93 S.E. 684, 687-88 (1917). However, "law of the case" has been applied in special situations to preclude a redetermination of issues affecting persons who were not parties to the earlier decision. For example, the concept of "privity" has been used as a basis for binding nonparties.[6] Another example of the careful application of "law of the case" is contained in *Zdanok v. Glidden Co., Durkee Famous Foods Division*, 327 F.2d 944, 952-53 (2d Cir. 1964). In *Zdanok*, the court applied the doctrine of "law of the case" to preclude the defendant from re-litigating a question of contract construction. The earlier adjudication of the issue had involved the *same defendant* but a different plaintiff. In rejecting the defendant's argument against application of "law of the case," Circuit Judge Friendly's opinion states, "we see no reason why it [law of the case] should be peremptorily excluded because of the presence of new parties *when the party against whom it is invoked was fully heard on a prior appeal* . . . ." *Id.* (emphasis added).

The touchstones of the constitutional application of "law of the case" to nonparties are the Due Process requirements of effective notice and opportunity to be heard. *Cf.* Note, Collateral Estoppel of Nonparties, 87 Harv. L. Rev. 1485, 1495-97 (1974). Without vigilant judicial protection of these fundamental requirements, the very basis of the adversary system is threatened. The Court should grant certiorari in order to define the

[6]The Fourth Circuit has held specifically that Frost and Dreisen were *not* in privity with Capital, the party affected by the District Court's May 4, 1971 decision imposing a constructive trust. App. F at 71a.

constitutional boundaries for the use of the judicially created doctrine of "law of the case" to bind nonparties. As suggested by the dissent to the opinion of the Fourth Circuit below, the "law of the case" rule which the Fourth Circuit imposed on Frost and Dreisen is not logically or constitutionally sound. App. A at 12a.

II.

SIGNIFICANT CONSTITUTIONAL QUESTIONS ARE RAISED BY THE FOURTH CIRCUIT'S REQUIREMENT THAT NEWLY JOINED PARTIES PRESENT NEW EVIDENCE IN ORDER TO GAIN REVERSAL OF A DECISION ADJUDICATING THEIR RIGHTS MADE WHEN THEY WERE NOT PARTIES

The Fourth Circuit justified its reliance upon "law of the case" by stating that Frost and Dreisen failed to introduce new evidence supporting a reversal of the earlier decision which had been affirmed on appeal. App. A at 4a. The rule requiring the production of new evidence on remand, when applied to *nonparties* to a prior decision, denies the full dimension of an opportunity to be heard and raises significant constitutional questions.

In *White v. Murtha*, 377 F.2d 428, 431-32 (5th Cir. 1967), the rule requiring new evidence on remand was discussed. The court stated that:

> [A] decision of a legal issue or issues by an appellate court establishes the 'law of the case' and must be followed in all subsequent proceedings in the same case in the trial court or on a later appeal in the appellate court, unless evidence on a subsequent trial was substantially different, controlling authority has since made a contrary decision of the law applicable to such issues, or the decision was clearly erroneous and would work a manifest injustice. (footnote omitted).

See also Lincoln National Life Insurance Co. v. Roosth, 306 F.2d 110, 112 (5th Cir. 1962), *cert. denied*, 372 U.S. 912 (1963).

As the dissenting opinion below recognizes, the requirement of presenting new evidence has never been applied in the situation where new parties have entered the case *after* the previous decision. Whatever salutory effects the rule may have when applied to parties to the earlier decision,[7] its application to nonparties raises significant Due Process issues.

The function of parties to a lawsuit is not merely to introduce evidence.[8] Parties are entitled to shape the course of litigation by various means including decisions as to the employment of particular arguments, choice of counsel and forum, determination of the advisability and order of presentation of claims and defenses, and participation in the development of trial strategies and tactics. The introduction of evidence may be a very small part of the process by which a party presents a case. Both practical and symbolic considerations support a broad interpretation of the constitutional dimensions of the

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[7] The practice of mechanically applying "law of the case" to adjudicate the rights of prior parties is subject to question. *Lincoln National Life Insurance Co. v. Roosth*, 306 F.2d 110, 115 (5th Cir. 1962) (Hutcheson, J., dissenting with Jones and Bell, JJ.). This Court should exercise its supervisory power over the lower federal courts by addressing the issue raised by this practice.

[8] This is especially true when the parties are defendants. Frost and Dreisen were defendants against the claims asserted by the Morrison Estate. As recognized by the dissenting Circuit Judge, the application of "law of the case" in the instant case "shifts the burden from Morrison's Estate, to prove its case as the proponent, to the defendants Frost and Dreisen to prove incorrect previous fact findings in a case to which they were not parties." App. A at 12a.

right to a "day in court" and a "fair opportunity to be heard." *See* Note, Collateral Estoppel of Nonparties, 87 Harv. L. Rev. 1485, 1497 (1974).

The instant case demonstrates the inequity involved in applying to nonparties the rule requiring new evidence. The decision adverse to Frost and Dreisen was rendered *prior* to their entry into the case. After they were made parties and had an opportunity to be heard, the District Court (on two separate occasions) entered decisions in favor of Frost and Dreisen. App. E at 41a; App. G at 78a. By reverting to an earlier adverse decision to finally adjudicate the case, the Fourth Circuit effectively denied Frost and Dreisen their day in court. Whether such a denial is justified and constitutionally permitted by operation of the doctrine of "law of the case" is a question which merits the attention and guidance of this Court.

CONCLUSION

For the reasons stated above, a writ of certiorari should issue to review the judgment and opinion of the Fourth Circuit.

Respectfully submitted,

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February 2, 1979

APPENDIX

APPENDIX A

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 75-1498

CAPITAL INVESTORS CO.,
Plaintiff,

NORMAN B. FROST, deceased, and
HARRY DREISEN,
Appellees,

v.

EXECUTORS OF THE ESTATE OF
ARTHUR R. MORRISON,
Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA,
AT ALEXANDRIA
Richard B. Kellam, District Judge

Argued October 3, 1977 Decided September 29, 1978

Before HAYNSWORTH, Chief Judge, WINTER and
WIDENER, Circuit Judges

Joseph B. Hyman (Echols & Hyman on brief) for Appellant;
Lee T. Ellis, Jr. (John A. Beck on brief) for Appellees.

PER CURIAM:

This is the fifth appeal in this diversity jurisdiction case.[1] Arthur R. Morrison, who was engaged in financial

[1] Our earlier opinions are reported at 484 F.2d 1157 (1973); 453 F.2d 1365 (1972); 387 F.2d 591 (1967); 350 F.2d 462 (1966).

controversy with his estranged wife, was the owner of valuable lands in Rosslyn, Virginia and in Brevard County, Florida. He contracted to convey those lands to Capital Investors Company, a shell corporation wholly owned by James T. Benn, for $1,100,000 represented by unsecured notes. Because of Mrs. Morrison's claims against the Virginia lands, the contract was renegotiated and a new agreement entered into affecting the Virginia lands alone. Notes were issued to Morrison and Mrs. Morrison in the amount of $500,000 each, while $100,000 was retained by Capital Investors to "clear the title" which was encumbered by a relatively small deed of trust and which was complicated by what purported to be a prior conveyance of the fee and by another instrument which purported to be a ninety-nine year lease.

In the course of clearing the title to the Virginia lands, the district judge required Benn to give the Morrisons deeds of trust to secure their notes. There was default in the payment of the ntoes, and the Morrisons repurchased the Virginia lands at a foreclosure sale.

At the time of the first contract between Morrison and Capital Investors, a deed was signed by Morrison conveying the Florida lands to Capital Investors, in return for which he received Capital Investors unsecured notes in the amount of $400,000.[2] Benn persuaded Morrison that he could not lawfully encumber the Florida lands to secure the payment of the notes of Capital Investors because the title was uncleared.[3]

Initially, the district court held there was no evidence of fraud on Benn's part. At the time, it was concerned

[2] Benn did put the certificate representing the capital stock of Capital Investors in escrow, but Morrison soon released it.

[3] There was a recorded deed from Morrison to another who was later held to have been a naked trustee.

solely with the Virginia lands and at the time there was no evidence of a number of transactions affecting the validity and the value of the notes of Capital Investors. Later, after a full trial before another district judge, it was found that no consideration had been paid for the conveyance of the Florida lands and that Capital Investors did not intend to comply with its obligations by paying the notes. He imposed a constructive or resulting trust upon the Florida lands, or the notes representing their proceeds. On appeal we affirmed that decision.

Shortly after issuing its notes aggregating $400,000 for the Florida property, Capital Investors sold the land to Do-Mor, Inc. for $460,000 of which $400,000 was represented by notes secured by a mortgage. Later, Capital Investors transferred the Do-Mor notes to another corporation owned by Benn and later to still another. One note in the face amount of $25,000 was paid by Do-Mor; another in the face amount of $50,000 was sold to Mrs. Morrison. The remaining two, aggregating $325,000, after default, were sold for $150,000 to a nominee of Norman B. Frost, who, in turn, sold a one-half interest in the notes to Harry Dreisen for $75,000.

After our affirmance of the judgment establishing a constructive or resulting trust, Frost and Dreisen intervened. The district judge then undertook to balance the equities between Morrison, on the one hand, and Frost and Dreisen, on the other hand, and, considering Frost and Dreisen untainted by Benn's machinations, he concluded that they should prevail. We reversed. We held that the Uniform Commercial Code controlled, and that, since the Do-Mor notes were in default at the time of their purchase by Frost, they took the notes subject to lawful claims against them. However, we rejected Morrison's contention the Frost and Dreisen were bound

by the earlier decision imposing a constructive or resulting trust upon the notes. They had not been parties to the litigation when that issue was heard and decided. We thought they should have an opportunity to relitigate the issue if they could produce additional relevant evidence.

On remand, Frost and Dreisen produced no new evidence, but did prevail upon the district judge to review his earlier decision imposing a trust upon the notes. At this time he found no fraud on Benn's part. Alternatively, he found that Morrison's claim to the Florida lands was foreclosed by a release purportedly signed by Morrison. He found that the release was supported by a consideration and effectively barred the claim.

I.

While we held that the strict rules of *res judicata* did not foreclose relitigation of the issue by Frost and Dreisen, who had not been parties to the litigation when the issue was decided, we did not intend for earlier findings and conclusions, which had been affirmed on appeal, to be overturned with no new evidentiary basis for it.[4] There was no infirmity in the earlier findings and conclusions. After their affirmance on appeal, the principles of the law of the case required adherence to them.

The principle is not absolute nor inflexible. In such cases courts have an inherent power to correct earlier error, if it becomes apparent, and to avoid injustice,

[4] *See* Virginia Electric & Power Company v. NLRB, 132 F.2d 390 (4th Cir. 1942), aff'd 319 U.S. 533 (1943); Stonega Coke Sign & Coal Co. v. Price 116 F.2d 618 (4th Cir. 1940).

but there is no such situation here. The evidence of Benn's fraud is compelling.

Benn persuaded Morrison to accept the unsecured notes of Capital Investors. There was no cash payment. He was careful not to obligate himself. He quickly had Capital Investors deed the land to Do-Mor, and then he stripped Capital Investors of its only assets, leaving it with no resources with which to pay anything on the notes given to Morrison. Do-Mor paid one note in the face amount of $25,000, but it is not clear that any of that got to Morrison. The $50,000 note which had been sold to Mrs. Morrison was subsequently paid by Frost and Dreisen. No payment was ever made on the remaining notes aggregating $325,000. The mortgage securing the payment of those Do-Mor notes has now been foreclosed by Frost and Dreisen, however, and they acquired title to the land in the foreclosure sale. What Benn did amply supports the finding that he never intended that the Capital Investors notes be paid; he diverted all of Capital Investors' assets and stripped it of all means of payment. In the process, what cash flowed to Capital Investors or to Benn, or to other controlled corporations probably was not passed on to Morrison. All of it certainly was not.

Benn was an accomplished fraud artist. On a plea of guilty, he was convicted in 1971 in the United States District Court of the District of Columbia of fraud by mail. In 1963, the Tax Court found him guilty of tax fraud. T.C. Memo 1963-151. In its opinion, the Tax Court referred to a pattern of acquiring valuable properties largely on the basis of notes which were, or became, worth less and which Benn never intended paying. The kind of complicated schemes in which he engaged are illustrated in the opinion of Judge Jones in

Sankin v. 5410 Connecticut Avenue Corporation, D.C.-D.C. 281 F. Supp. 324 (1968), in the opinion of Judge Fulton in Walsh v. Continental Insurance Underwriters Inc., (S.D. of Fla. No. 63-576-Civ-CF, 1965) and in the opinion of Judge Hoffman in Freehill v. Benn (E.D. of Va., No. 3421, 1969). He had the capacity of persuading even sophisticated business people to place their trust in him. Though he was not a lawyer, he dealt in legalisms. He convinced Morrison that he was a "legal genius" and a helping friend. What he did to Morrison, however, was in the pattern disclosed in the court cases. When he stripped Capital Investors of its assets and devoted them to his own use without paying the Morrisons, he clearly established that his intention, from the beginning, was not to pay the Morrisons.

Frost, about whom the district judge was concerned, was not entirely an innocent, unsuspecting victim of deception. Several reasons for this are catalogued in the opinion reported at 484 F.2d 1157 at pages 1164 and 1165. Frost, now deceased, was a reputable lawyer in the District of Columbia, but he knew Benn. His firm represented some of Benn's associates in the *Sankin* case. Indeed, he paid Benn only $100,000 for the two notes, the remaining $50,000 of the price being a credit for legal fees due Frost's firm by Benn's associates, the payment of which Benn had guaranteed. From the facts in the *Sankin* case, Frost was bound to have known the kind of man Benn was.

Under the circumstances, we think the district judge was required to adhere to his earlier findings and conclusions that a constructive or resulting trust did arise.

II.

Within three months of the initial transaction, Morrison purportedly signed a release acquitting Capital Investors and Benn of all claims by him. Released were any claims to the Florida lands and to any payments by Do-Mor on its notes. The release was under seal and delivered in Virginia. The district court held that Morrison's estate had failed to prove there was no consideration for the release, and he concluded that it was valid and binding.

Benn never testified that he gave any actual consideration for the release. He claimed generally that he had given or paid Morrison some $28,500, though Morrison testified it was no more than $4,000. The contract obligated Benn to pay to Morrison a minimum of $25,000 a year, for living expenses, until the titles were cleared. Benn produced receipts purportedly signed by Morrison for cash payments in 1963 of $30,537, but, of that, $12,500 was payment for some corporate stock, according to Benn's testimony. Thus, only $17,500 was paid to Morrison by Benn in 1963 for the real estate, and that would have been upon his obligation to make advances for Morrison's expenses each year up to $25,000. The release was dated August 6, 1963, and the nearest date to that date of any of the receipts is July 15, 1963, when Morrison acknowledged the receipt of $2,037.[5] There was no receipt for any payment by Benn in 1963 after July 15. Even if it be assumed that some portion of whatever monies Benn funneled to Morrison was purported consideration for the release,

[5]Morrison, of course, denied that he received more than approximately $4,000. He specifically denied receipt of the $10,000 payment for which Benn produced a receipt.

the consideration was grossly inadequate, for the Morrisons held notes aggregating $1,000,000, and the lands were thought by Morrison to be worth that.

Defensively, it is suggested that under Virginia law the seal on the release conclusively imports consideration, at least when the litigation is between the original parties.[6] There are exceptions, however, when different parties are involved, and possibly when proceedings are in equity, as these are.[7] Surely, however, there is an exception in equity when an application of the strict rule of the common law would perpetrate a fraud or grave injustice.

In *Cooper v. Gregory*, 191 Va. 24, 60 S.E.2d 50, the holders of contingent remainders under the will of their father purported to convey a portion of the land in fee to their sister in exchange for a promise to care for another, mentally incompetent, sister as long as the incompetent lived. The agreement was under seal. Apparently the sister, as long as she lived, did take care of the incompetent, but after her death the representatives of her estate declined to do so longer. The purported grantors of the land sought to enforce performance by the sister's estate of the agreement she had made. The Supreme Court of Virginia held the agreement unenforceable despite the seal. First, it was said that the purported grantors of the land had only contingent remainders in it so long as their mother lived, and they were without power to make a valid conveyance. Moreover, it was said, if anything was conveyed, its value was

[6] Norris v. Barbour, 188 Va. 73, 51 S.E.2d 334 (1949); Turner v. Hall, 128 Va. 247, 104 S.E. 861 (1920).

[7] *See* Branch v. Richmond Cold Storage Inc., 132 S.E. 848, 851 (1926), in which it is flatly stated that the common law rule that a seal imports consideration is not the rule in equity.

so slight in comparison with the financial burden assumed by the sister that it would be unconscionable to enforce the bargain. The Supreme Court of Virginia concluded:

> "Equity will not lend its aid to the performance of such an unconscionable bargain—certainly not in a case of this nature where the other contracting parties surrendered no rights and suffered no detriment."

Here there was no proof that any consideration was paid for the release.[8] The dates and the amounts of the payments Benn claimed to have made are known, and none of them can be related to the release. If any at all was paid, it was a pittance in contrast to the claim released. The release purports to be a release of all claims, though there is specific reference to the Florida lands and the Do-Mor notes. If construed to apply to the Florida lands alone, the claim purportedly released was still for more than $400,000. The gross disparity between the amount of the claim and any possible consideration for the release makes enforcement of the bargain outrageously unconscionable.

Benn was an experienced con artist, once convicted of tax fraud. We do not know how he did it, but for a while at least, he seemingly could persuade Morrison to do anything Benn wished. He persuaded him to sell him the Virginia and Florida lands for unsecured notes (he gave the Morrisons a deed of trust on the Virginia lands only because Judge Butzner, after the first trial,

[8] The presence of the seal would place the burden upon Morrison to go forward with evidence to show the absence of consideration for the release, but there is no absence of evidence. Morrison testified that he never got more than $4,000 from Benn, and the receipts show exactly what Benn claimed to have paid Morrison and when.

required him to do it). He persuaded Morrison that there was some legal inhibition in Florida which prevented his securing payment of the notes arising out of the transfer of title to the Florida lands. Benn had placed the certificate representing the stock of Capital Investors Company in escrow, supposedly to give Morrison some little security, though it was precious little, but he soon persuaded Morrison to agree to a release of that escrow agreement. If Morrison signed this purported release so soon after the initial agreement with Benn, it is but one more testimonial of Benn's persuasive power over him. But it was the same kind of persuasive power exercised by Benn over other victims, as the reported cases show.

Since there was no actual consideration for the release, or, if any, so little as to make enforcement of the release unconscionable, we find under *Cooper v. Gregory* that under Virginia law the seal should be disregarded and the release declared invalid.

Since Frost and Dreisen have converted their ownership of the Do-Mor notes into ownership of the land, the Morrisons now have a constructive or resulting trust in the Florida land and are entitled to an order requiring the defendants to convey it to them. However, the defendants will be entitled to some credits. They paid the $50,000 Do-Mor note which had been purchased by Mrs. Morrison. Supposedly they have paid taxes, and there may be other items of expenses which equitably may be chargeable to the Morrisons upon a reconveyance of the land. On the other hand, they should be accountable for any income. This will necessitate some accounting and further proceedings in the district court.

REVERSED AND REMANDED.

WIDENER, Circuit Judge, dissenting:

I respectfully dissent because the opinion of the panel confessedly does not give any weight to the current fact finding of the district court; I think it does not other than formally follow *Pennoyer v. Neff*, 95 U.S. 714 (1877); and I think it departs from established Virginia precedent which controls us here. My disagreement with the panel on its factual treatment of the case is somewhat intertwined with its treatment of *Pennoyer v. Neff*, as will be apparent. My disagreement with it on its failing to follow Virginia precedent is self-evident from this dissent.

I

With respect to *Pennoyer v. Neff*, a previous panel, as the majority mentions, had sent this case back for another trial so far as Frost and Dreisen were concerned, because they were not parties to the adverse decision against them. Nevertheless, despite different attorneys asserting different interests from a different point of view, this court now disposes of the case on "earlier findings and conclusions, which had been affirmed on appeal." While there may not have been any new evidence taken, the evidence presented to the district judge was different, and that is not denied. It not only included different matter, but was presented from the view of Frost and Dreisen, not parties to the case at the time of the adverse findings which they now find to be binding.[1] The very reason for the rule of *Pennoyer v. Neff*, that a man shall not suffer a judgment against him unless he is properly a party to the cause, is violated by the majority

[1] No point is made of the absence of Frost and Dreisen from earlier proceedings.

here, for the attorneys for some other party had no interest in protecting the rights of Frost and Dreisen. Rather, should it have served the purposes of their clients, they were ethically obligated to make absent parties appear in as bad a light as possible.

I think the rule the court today announces of requiring a new evidentiary basis for a new party, rather than a reconsideration of the evidence in the light of the fact that there are new parties, does not withstand either logical or constitutional analysis. Reconsideration of the evidence in the light of the fact that there were new parties is exactly what the district judge did, and I think his findings of fact are entitled to the same consideration as if they had been parties in the first place. Merely stating, as the panel does, that the first decision of the court finding a resulting trust should be affirmed because there is no new evidentiary basis, meaning no additional evidence, as I have said, I think is a misapplication of the rule of *Pennoyer v. Neff* which should require at the very least a reconsideration of all the evidence as was, I think, correctly done by the district judge. The panel decision, erroneously I think, shifts the burden from Morrison's estate, to prove its case as the proponent, to the defendants Frost and Dreisen to prove incorrect previous fact findings in a case to which they were not parties. That the panel decision clearly does just this is shown by its finding, not that the district judge was clearly erroneous, but that "he was required to adhere to his earlier findings and conclusions." Slip op. p. 8.

Along this line, another thing needs mention. The panel relies on "law of the case" to require "adherence to" the fact finding previous to the time Frost and Dreisen were parties to the case. Slip op. p. 5. I do not

agree for I do not think previous fact finding can bind a person who is not a party to the case to his detriment in the context presented here absent at the very least a complete reconsideration of the record as a whole plus the opportunity to present evidence after the absent defendant is made a party to the case.

Finally, the majority cites *Virginia Electric & Power Co. v. NLRB*, 132 F2d 390 (4th Cir. 1942), aff'd 319 U.S. 533 (1943), and *Stonega Coke Sign & Coal Co. v. Price*, 116 F2d 618 (4th Cir. 1940), for the proposition that the district court was bound by its earlier findings. I think neither of these cases supports such a rule. In both *Virginia Electric* and *Stonega Coke* the same parties were before the court both before and after the remand. Neither case, I suggest, has anything to do with the binding application of prior findings of fact to persons who were not parties to the action at the time the fact findings were made. The affirmance of the *Virginia Electric & Power* case, I note, did not discuss the point under consideration.

II

For the fith time in the thirteen year history of this diversity case, we consider issues relating to a 1963 land conveyance between Arthur R. Morrison and Capital Investors Company (Capital). Here, we are most directly concerned with the ownership of two notes, in the total amount of $325,000, as the balance of the proceeds for the conveyance of land in Brevard County, Florida, from Capital to Do-Mor, Inc. Capital initially purchased the land from Morrison, whose estate claims the notes as the beneficiary of a constructive trust.

The issues before us are whether the district court was clearly erroneous in finding that: (1) valid con-

sideration supported the sale of the Florida land from Morrison to Capital, (2) Capital, through its sole owner, James T. Benn, was not guilty of fraud in the purchase of the property from Morrison, and (3) a release executed by Morrison with respect to all claims arising out of the sale of the Florida property was supported by valid consideration.[2]

On May 18, 1963, Morrison entered into a contract with Capital for the sale of lands located in Arlington County, Virginia, and Brevard County, Florida, for the stated consideration for the conveyance of $1,100,000, which was to be paid by a "judgment note." Complications ensued, however, that threatened to prevent Morrison from conveying good title to the Virginia property. Pursuant to an earlier marital property settlement, Mrs. Morrison, who was not a party to the May agreement, held notes in the amount of $180,000 secured by a deed of trust on that property. In July 1963, the notes were in default, and Mrs. Morrison purported to take action to have title to the property vest in her.

Because of this difficulty with Mrs. Morrison, Morrison was forced to enter into a subsequent agreement concerning the land with Capital, this time with Mrs. Morrison as a signatory. This agreement was dated July 29, 1963. The total stated consideration was the same as in the previous contract, to be equally divided between the Morrisons (with $100,000 to be used to clear the title), but the agreement appeared to refer only to the Virginia property.

By order of the district court dated June 29, 1965, fee simple title to the Virginia property was quieted

[2]Arthur Morrison died on January 24, 1970. He and Mrs. Morrison were divorced November 29, 1962.

in Capital. This appeal directly concerns the Florida property alone.[3] That land was conveyed to Capital by deed dated May 18, 1963, pursuant to the original May 18, 1963 contract. On June 21, 1963, Capital conveyed the Florida realty to Do-Mor, Inc., which, in addition to releasing trusts of $60,000, issued four purchase money notes in the total amount of $400,000, secured by a purchase money mortgage.[4] That mortgage and two of the Do-Mor notes were subsequently purchased by Norman B. Frost and Harry Dreisen in 1965.

The estate of Morrison claims that Capital held the Do-Mor notes as a constructive trustee for Morrison's benefit in 1963 on account of Capital's fraud or unjust enrichment in the initial conveyance of the Florida land to Capital.[5] If the estate were able to establish

[3]This litigation was initially instituted in 1963 by Capital to quiet title to the Virginia property. The issues we decide today arise by way of counterclaim filed by Morrison in 1965.

[4]Note No. 1, for $25,000, was paid by Do-Mor; Note No. 2, for $50,000, was sold to Mrs. Morrison and was subsequently paid by Frost and Dreisen. This appeal concerns the ownership of notes 3 and 4, for $100,000 and $225,000 respectively.

[5]The record is clear that default occurred on the notes issued by Capital as payment for the Virginia and Florida properties. Capital claims to have paid as much as $28,500; Morrison denies receiving more than about $4,000—both figures far from the purchase price in excess of one million dollars. This default forms one of the bases of Morrison's executors' claim of entitlement to a constructive trust on the ground of Capital's unjust enrichment. They also claim that the Florida land was conveyed without consideration because they say the agreement of July 29, 1963 applied only to the Virginia property and superseded the earlier agreement that undeniably pertained to both the Florida and Virginia lands.

It is quite noteworthy that the Morrisons foreclosed on a later obtained deed of trust they held on the Virginia property in 1970, which was sold for $700,000 to themselves. Morrison's executors obtained a deficiency judgment for about $400,000 against Capital in 1971.

successfully that Morrison was entitled to such a constructive trust, the claim is that it would prevail over the interest of Frost and Dreisen in the notes or the Florida land itself.[6] This, they say, is because we held the last time this case was before us that Frost and Dreisen were not holders in due course of the Do-Mor notes under §3-306 of the Uniform Commercial Code, and hence took the notes from Capital subject to all valid claims on the notes against Capital. 484 F2d 1157 (4th Cir. 1973). In the last appeal, we remanded to the district court to determine whether, as between Morrison on the one hand and Frost and Dreisen on the other, Morrison was entitled to a constructive trust in the two notes in question.[7]

On remand the district court held that the estate failed to meet its burden of proof on the issue of a constructive trust. Specifically, it found that the 1.1 million dollar purchase price was consideration for both the Virginia and Florida properties, not for the Virginia property alone. The district court also held that it was

[6] Following Do-Mor's default on notes 3 and 4, Frost and Dreisen foreclosed on the Florida property, and purchased it at the foreclosure sale. The notes having been satisfied in part, at least, from the proceeds of the sale, Morrison's executors apparently now claim either the property itself as standing in place of the notes, or the benefit of any deficiency still owing by Do-Mor.

[7] Our most recent decision in this case reversed the district court's 1972 judgment that denied a constructive trust on the basis of equitable principles of real estate law, favoring Frost and Dreisen as good faith purchasers without notice. We held that the case was controlled by the Uniform Commercial Code provisions dealing with the purchase of negotiable instruments.

We also held that the district court's 1971 opinion, in which Morrison's executors prevailed in their constructive trust claim, was not controlling since Frost and Dreisen were not parties to the litigation at that time.

necessary to prove fraud before a constructive trust should be imposed and that the estate failed to meet its burden of proving fraud on the part of Benn, the owner of Capital. While Morrison concededly never received full payment on the notes issued by Capital for the purchase price, to the extent those notes were unsecured Morrison was merely a general creditor of Capital with claim for payment of the notes which has been prosecuted to a conclusion.

III

The estate claims that the district court committed error in requiring proof of fraud to establish a constructive trust. It asserts that the constructive trust remedy can be administered with considerably more flexibility, specifically where unjust enrichment is demonstrated. The district court stated that "[t]he basis of a constructive trust is fraud, actual or constructive," citing cases, and imposed upon the appellant the burden of proving fraud by "clear and convincing evidence." *Sutton v. Sutton,* 194 Va. 179, 72 S.E.2d 275 (1952); *Malbon v. Davis,* 185 Va. 748, 40 S.E.2d 183 (1946).

There are statements in the Virginia cases, relied upon by the district court, suggesting that either fraud or breach of a fiduciary duty is requisite to the imposition of a constructive trust. *Miller v. International Union of Brewery Workers,* 187 Va. 889, 48 S.E.2d 252 (1948); *Porter v. Shaffer,* 147 Va. 921, 133 S.E. 614 (1926). While there is persuasive authority that unjust enrichment may constitute a ground for the creation of a constructive trust.[8] I would find it unnecessary to express an

[8] See *Buchanan v. Brentwood Fed. Savings & Loan Ass'n,* 320 A.2d 117, 126-7 (Pa. 1974); *Annon v. Lucas,* 185 S.E. 2d

[footnote continued]

opinion on the matter, for I would hold that the district court was not clearly erroneous in finding that the sale of the Florida land was supported by valuable consideration. This compels the conclusion that, absent fraud, there was no unjust enrichment in this case as a matter of law sufficient to justify a constructive trust. There was at most a basis for a suit for damages, and this claim, if it ever existed, is co-extensive with the $400,000 judgment already obtained in 1971 against Capital by Morrison's estate and the Morrisons' foreclosure upon the purchase money notes.

The contract of May 18, 1963, pursuant to which Morrison agreed to convey the Florida property, recites a consideration for the conveyance of 1.1 million dollars, in the form of a judgment note payable within five years and bearing six percent interest.[9] As a matter of basic contract law, mutual promises constitute a valuable consideration in a bilateral contract. *Adams, Payne & Gleaves v. Indiana Wood Preserving Co.*, 155 Va. 18, 154 S.E. 558 (1930); *Bernstein v. Bord*, 146 Va. 670, 132 S.E. 698, 699-700 (1926). That the notes executed and delivered by Capital for the payment of the purchase price to Morrison constituted a consideration for the conveyance and a legally binding obligation needs no further elaboration than reference to the Morrisons' foreclosure on those notes and the obtaining of a deficiency judgment by Morrison's estate.

Morrison's estate's argument that the July 29, 1963 contract superseded the earlier agreement and left

343, 352 (W. Va. 1971); D. Dobbs, *Handbook on the Law of Remedies*, §4.3 at 246 (1973); 4 Scott, *The Law of Trusts* §462 at 3103 (2d ed. 1956); 31 *Va. L. Rev.* 962 (1945).

[9]Morrison also took all of the capital stock of Capital in escrow as collateral to secure the payment of the purchase price.

the Florida conveyance unsupported by consideration is without merit. The district court, with all interested parties before it,[10] unequivocally found that the purchase price of the Virginia and Florida properties together was 1.1 million dollars, and that the July agreement reaffirmed the earlier agreement and conveyance. This finding, in the words of the district court, "is established beyond doubt." The district court's interpretation of the July transaction, that it was intended solely to secure Mrs. Morrison's necessary cooperation in fulfilling the obligations of the May contract, and not to displace that agreement, is amply supported by the record.

In order for Morrison's estate to rely upon the breach of an arms-length contract as the basis for a constructive trust, it is necessary to prove that the breaching party never intended to perform his contractual obligations—a circumstance which may constitute fraud. It had the burden of proving fraud by clear and convincing evidence. *Malbon v. Davis*, 185 Va. 748, 40 S.E.2d 183, 187 (1946). The district court found that "not a particle" of evidence had been presented by appellants to prove fraud since 1964, when Judge Butzner, sitting as a district judge in this case, came to the conclusion that neither the May 1963 nor the July 1963 contracts and conveyances were procured by actionable fraud.[11] Thus,

[10]The district court's 1971 holding that the appellants were entitled to a constructive trust was based on its finding, with opposing parties not before it, that the Florida conveyance was not supported by consideration. The finding was reconsidered by that court when both sides were in court and represented.

[11]While Judge Butzner's finding of no fraud on the part of Capital, affirmed by this court in 360 F2d 462 (4th Cir. 1966), may be res judicata on that issue against those who were parties

[footnote continued]

two district judges, after full hearings in the protracted history of this litigation, have rejected the contention that Capital committed fraud in its transactions with Morrison.

I have examined the statements in the panel opinion intended to establish Benn's fraud (meaning Capital), and note that they consist largely of a list of unsavory activities from Benn's life over the past fifteen years. It should not be our province to pass judgment on Benn's life,[12] only to review whether the district court's conclusion was clearly erroneous with respect to a particular sale of land in 1963. I conclude that it was not. Benn and Morrison testified orally before Judge Butzner, who found no fraud. Judge Kellam found no evidence of it after Judge Butzner's finding. I do not think the findings are clearly erroneous. FRCP 52(a).

What is left of the case, then, in my view, is a situation in which notes taken in consideration for the sale of land were not paid. The transaction was untainted by fraud and supported by a valuable consideration. Nothing

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to that proceeding, or may work an estoppel in other situations, I would not find it necessary to rely on that principle nor similarly upon the result of a suit in Florida to which Morrison was a party which apparently held, after the conveyance to Capital, that he had no further interest in the Florida land. But a reliance on the finding by Judge Butzner that Capital was free of fraud in 1963 in a case in which Capital *was* a party is much more logical to me than the present finding thaf Frost and Dreisen are bound by a finding that Benn was guilty of fraud, or like activity, in a case in which they were *not* parties.

[12] None of the activities of Benn listed on p. 7 of the slip opinion, for example, are even remotely connected to the transactions at issue here. The panel relies on them for its fact finding. I think it is in error with perhaps the sole exception of a criminal conviction of tax fraud as going to credibility, and even that is not spelled out.

prevented Morrison from taking a purchase money deed of trust on the real estate as security for payment of the purchase price as he agreed to take the Capital stock as security. There is simply no theory under which a mere failure to pay a debt can justify the imposition of a constructive trust. *McKee v. Paradise*, 299 U.S. 119 (1936); *Cherno v. Dutch American Mercantile Corp.*, 353 F2d 147, 154 (2d Cir. 1965); see *Porter v. Shaffer*, 147 Va. 921, 133 S.E. 614 (1926). Were a contrary rule to prevail, its effect would often be to create an unwarranted preference in favor of one general creditor over others. *McKee*, p. 123.

IV

As an alternate ground for its holding, the district court relied upon a release executed by Morrison on August 6, 1963, releasing Capital and Benn from all claims arising out of the sale of the Florida property. Appellants seek to avoid the effect of this release by arguing that it was unsupported by consideration, notwithstanding that it acknowledges receipt of valuable consideration and was executed under seal.

Under Virginia law, a sealed instrument generally conclusively imports consideration so far as the parties[13] to the agreement are concerned. *Norris v. Barbour*, 188 Va. 723, 51 S.E.2d 334 (1949); *Turner v. Hall*, 128 Va. 247, 108 S.E. 861 (1920); see *Northwestern Nat'l Ins. Co. v. Cohen*, 138 Va. 177, 121 S.E. 507, 508 (1924); *Ferries Co. v. Brown*, 121 Va. 13, 92 S.E. 813 (1917). While this rule does not necessarily obtain when the instrument is attached for fraud, and it is true that equity will look to the substance rather than

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[13] When a party has died, the rule may be relaxed. See e.g. *Norris* and *Cooper*, infra.

the form of a transaction to prevent a fraud, see *Cooper v. Gregory,* 191 Va. 24, 60 S.E.2d 50 (1950), Morrison's executors, with the burden of producing evidence upon them, failed to show that Capital obtained the release in a fraudulent manner, or indeed that the release was in any way irregular. The district court's conclusion that the release was supported by valuable consideration is in accord with applicable law, is based on facts supported by the record, and is not clearly erroneous. FRCP 52(a).

The case of *Woody v. Schaaf,* 106 Va. 799, 56 S.E. 807 (1907), is very nearly indistinguishable on its facts from the case at hand. There, an obligation under seal given for an antecedent debt was in issue after the death of the maker of the obligation. The court held that, as against the maker's estate, the seal was conclusive evidence of the debt, and, as against an insurance company involved which was defending on the ground its policy on the maker's life was a wager policy, the seal was *prima facie* evidence.

Prima facie evidence, in Virginia, shifts the burden of going forward with the evidence, *Witt v. Merricks,* 210 Va. 70, 168 S.E.2d 517 (1969). It is evidence which on its first appearance is sufficient to raise a presumption of fact or establish the fact in question unless rebutted. It imports that the evidence produces for the time being a certain result but that the result may be repelled. *Babbitt v. Miller,* 192 Va. 372, 64 S.E.2d 718 (1951).

Here, applying the rule of *Woody* rigidly, the release under seal would conclusively establish consideration against Morrison's estate. But, even assuming for argument that Morrison's estate had some kind of equity to place it in the position of those in *Norris* and *Cooper* who sought to avoid the effect of consideration imported

by a seal, the instrument under seal nevertheless established *prima facie* evidence of consideration. The district court, I think correctly, held that Morrison's estate had failed to prove there was no consideration, which furnishes an additional reason for its conclusion. Its finding is supported by the record.

The majority here, in a case in which the person who has executed a release under seal has died, wrongfully places the burden of proof on those claiming the release is valid, rather than those claiming the release is invalid, a legal proposition I think exactly contrary to established Virginia precedent on the very point.

APPENDIX B

[Filed March 29, 1977]

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 75-1498

CAPITAL INVESTORS COMPANY,

Plaintiff,

NORMAN B. FROST, deceased, and
HARRY DREISEN,

Appellees,

v.

EXECUTORS OF THE ESTATE OF
ARTHUR R. MORRISON,

Appellant.

ORDER

We are convinced by the petition for rehearing filed by attorneys for appellees on March 17, 1977, that we acted improvidently in reversing our prior decision without allowing a response to appellants' petition for rehearing. Rule 40(a), Federal Rules of Appellate Procedure. Technically, the rule also applies to this request, but we view the prior petition for rehearing filed by appellants as a sufficient exposition of the opposing viewpoint. We think the posture of the case is now such that we should start over.

Accordingly, it is ordered that the opinion on petition for rehearing dated March, 4 1977, and our prior opinion entered November 24, 1976, are withdrawn. It is further ordered that the case be set down for oral reargument

and that counsel be requested to file supplementary briefs, not to exceed 15 pages, on a briefing schedule to be established by the Clerk.

After hearing reargument and considering supplemental briefs, we will then either reinstate our opinion of November 24, 1976, *or* our opinion of March 4, 1977, or file a new opinion, as may seem just and proper.

Chief Judge Haynsworth and Judge Widener join and concur in this order.

/s/ [Signature]
United States Circuit Judge

APPENDIX C

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 75-1498

CAPITAL INVESTORS COMPANY,

Plaintiff,

NORMAN B. FROST, deceased, and
HARRY DREISEN,

Appellees,

v.

EXECUTORS OF THE ESTATE OF
ARTHUR R. MORRISON,

Appellant.

ON PETITION TO REHEAR AND RECONSIDER OUR DECISION ENTERED NOVEMBER 24, 1976

Argued: December 3, 1975 Decided: March 4, 1977

Before HAYNSWORTH, Chief Judge, and CRAVEN and WIDENER, Circuit Judges

Joseph B. Hyman (Echols and Hyman on brief)
for Appellant
John A. Beck and (Lee T. Ellis, Jr. on brief)
for Appellees

PER CURIAM:

On petition of counsel for the executors of the estate of Arthur R. Morrison, we withdraw the decisional portions (Parts I and II) of our prior opinion entered November 24, 1976, retaining the statement of the case by Judge Widener and incorporating it herein by reference. That statement accurately frames the questions for decision on this fifth appeal, and also contains references to the previously published opinions. All of them together tell more than anyone wants to know about what a tangled web one can weave who practices to deceive. It is our *Jarndyce*[1] and we sometimes wonder why it was visited upon us, and we wonder even more whether we can ever end it.

I. Was there valid consideration for the sale of the Florida land from Morrison to Capital? No.

In an opinion by Judge Russell, 484 F.2d 1157, 1159 (4th Cir. 1973), we have previously noticed that after a full hearing in March 1971, the district court

> found specifically that Capital had not "paid any consideration for the Florida properties" and that Capital "held the assets described, transferred and conveyed as a constructive or resulting trustee.
>
> All of the properties were owned by Mr. Morrison. No consideration was paid by Capital. Mr. Morrison is entitled to have all of the property returned to him, or the proceeds therefrom, subject to the right of any bona fide transferee."

We view the foregoing as the law of the case, subject only to such modification as might be supported by substantial evidence at the more recent hearing conducted pursuant to our remand. Nothing was developed on remand before the district court except what was known previously: that a convicted fraud artist named Benn had talked Morrison into accepting unsecured notes of an empty-shell corporation controlled and owned entirely by Benn, and that there is considerable doubt that Benn

[1] C. Dickens, *Bleak House* (1853).

or his creature corporation ever intended to pay anything for the property. The findings of fact of the district judge dated May 4, 1971, are supported by substantial evidence; his subsequent, exactly contrary finding is without evidentiary support and is clearly erroneous.

II. Was Capital, through its sole owner, James T. Benn, guilty of fraud in the purchase of the property from Morrison? Yes.

We think so. Years ago we noted that Frost himself had conceded that Benn's operations were "unethical." We also noted that Frost would not take an assignment of the notes in his own name because he did not wish his name associated with the notes. And he purchased the notes at a considerable discount and in a rather peculiar manner, all of which is catalogued in footnote 14 of our prior opinion, 484 F.2d at 1165. Benn's methods and patterns of fraudulent operation are well established by the record including a criminal conviction for tax fraud. We have previously noted that Capital Investors Company was "a corporate 'shell' owned and controlled completely by Benn, and which may be considered legally as identical with Benn." *Id.* at 1158. Thus Capital's promissory notes are the same as Benn's notes but with one significant difference: Benn was not obligated to pay them, and Capital had no property with which to do it. By itself such an arrangement by a person (Benn) who claimed to be worth ten million dollars is itself highly suspect and suggests fraud. But most significantly, Benn had Capital give its notes to Morrison and then stripped Capital of *all* assets by transferring the Do-Mor notes to himself. Such a sequence of events is per se fraudulent.

III. Was the release executed by Morrison with respect to all claims arising out of the sale of the Florida property supported by valid consideration? No.

There is some evidence in the record that Morrison received $4,000 (according to him) or $28,500 for the

release. But the district court did not find that there was any payment for the release and related these relatively paltry sums (without deciding which was paid) to payment on the Capital promissory notes. The district court reasoned that because the instrument was under seal and purported a consideration, that alone would suffice to support it. Erroneously, the district court stated that not a particle of evidence had been presented on the issue of consideration. On the contrary, even the litigants agree that no payment greater than the alleged $28,500 was ever paid Morrison. We noted in one of our prior opinions:

> So far as the release is concerned--the other matter raised by Frost and Dreisen, it is the position of the estate that there was either a want or failure of consideration. While the District Court did not clearly rule on this contention of the estate, the fact that it did not predicate its conclusion on the release would suggest that it considered the position of the estate well taken.

484 F.2d at 1163.

That would certainly seem to be so because, if Judge Kellam had considered the release legally binding in March 1971, he would surely have ended the lawsuit on that ground rather than resting his decision on equitable principles of law. After the most recent remand, despite a specific request pursuant to Rule 52(b) that the district court identify what consideration supported the release, there was no such finding. Even if Benn told the truth and actually paid Morrision $28,500, which seems highly doubtful, we think such an amount is insufficient to support the release of entitlement to notes in the face amount of $325,000 and now probably worth nearer a half million dollars including interest.

On remand the district court is instructed to enter judgment that the executors of the estate of Arthur R.

Morrison are owners of the two Do-Mor notes in the total face amount of $325,000 as the balance of the proceeds for the conveyance of land in Brevard County, Florida, from Capital to Do-Mor, Inc. Since Morrison admitted receiving $4,000, a cross-judgment will be entered against the executors and in favor of the appellees in that amount.

REVERSED AND REMANDED.

WIDENER, Circuit Judge, dissenting:

I respectfully dissent for the reasons stated in the prior opinion of the court filed in this appeal, ___ F2d ___ (4th Cir. 1976).

Since the majority seems insistent on looking to Benn's personal character for an answer rather than to legal principles, a reiteration of the reasons given for our previous holding would be an exercise in futility.

I cannot help but note, however, that the court's new opinion makes no effort whatever to deal with the effect of the release under controlling Virginia law, discussed at some length in our prior opinion. One can only speculate that the reason for this omission is the lack of an answer to the proposition there stated, and indeed I suggest there is none. The authority cited in the petition for rehearing barely touches the problem, much less gives grounds for a different answer.

APPENDIX D

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 75-1498

CAPITAL INVESTORS COMPANY,
Plaintiff,

NORMAN B. FROST, deceased and HARRY DREISEN,
Appellees.

v.

EXECUTORS OF THE ESTATE OF ARTHUR R. MORRISON,
Appellant.

Appeal From The United States District Court For The Eastern District of Virginia, At Alexandria
(Richard B. Kellam, District Judge)

Argued: December 3, 1975 – Decided: November 24, 1976

Before HAYNSWORTH, Chief Judge, and CRAVEN and WIDENER, Circuit Judges

Joseph B. Hyman (Echols and Hyman on brief) for Appellant

John A. Beck and (Lee T. Ellis, Jr. on brief) for Appellees

WIDENER, Circuit Judge:

For the fifth time in the thirteen year history of this diversity case, we consider issues relating to a 1963 land conveyance between Arthur R. Morrison and Capital Investors Company (Capital).[1] Here we are most directly concerned with the ownership of two notes, in the total amount of $325,000, as the balance of the proceeds for

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[1] Our prior opinions are reported in 484 F2d 1157 (1973); 453 F2d 1365 (1972); 387 F2d 591 (1967); 360 F2d 462 (1966). They will provide a more complete account of the history of the case in its aspects not directly relevant to this appeal.

the conveyance of land in Brevard County, Florida, from Capital to Do-Mor, Inc. Capital initially purchased the land from Morrison, whose estate claims the notes as the beneficiary of a constructive trust.

The issues before us are whether the district court was clearly erroneous in finding that: (1) valid consideration supported the sale of the Florida land from Morrison to Capital (2) Capital, through its sole owner, James T. Benn, was not guilty of fraud in the purchase of the property from Morrison,[2] and (3) a release executed by Morrison with respect to all claims arising out of the sale of the Florida property was supported by valid consideration. We affirm.

On May 18, 1963, Morrison entered into a contract with Capital for the sale of lands located in Arlington County, Virginia, and Brevard County, Florida, for the stated consideration for the conveyance of $1,100,000, which was to be paid by a "judgment note." Complications ensued, however, that threatened to prevent Morrison from conveying good title to the Virginia property. Pursuant to an earlier marital property settlement, Mrs. Morrison, who was not a party to the May agreement, held notes in the amount of $180,000 secured by a deed of trust on that property. In July, 1963, the notes were in default, and Mrs. Morrison purported to take action to have title to the property vest in her.

Because of this difficulty with Mrs. Morrison, Morrison was forced to enter into a subsequent agreement concerning the land with Capital, this time with Mrs. Morrison as a signatory. This agreement was dated July

[2] Arthur Morrison died on January 24, 1970. He and Mrs. Morrison were divorced November 29, 1962.

29, 1963. The total stated consideration was the same as in the previous contract, to be equally divided between the Morrisons (with $100,000 to be used to clear the title), but the agreement appeared to refer only to the Virginia property.

By order of the district court, dated June 29, 1965, fee simple title to the Virginia property was quieted in Capital. This appeal directly concerns the Florida property alone.[3] That land was conveyed to Capital by deed dated May 18, 1963, pursuant to the original May 18, 1963 contract. On June 21, 1963, Capital conveyed the Florida realty to Do-Mor, Inc., which, in addition to releasing trusts of $60,000, issued four purchase money notes in the total amount of $400,000, secured by a purchase money mortgage.[4] That mortgage, and two of the Do-Mor notes, were subsequently purchased by Norman B. Frost and Harry Dreisen in 1965.

The estate of Morrison claims that Capital held the Do-Mor notes as a constructive trustee for Morrison's benefit in 1963, on account of Capital's fraud or unjust enrichment in the initial conveyance of the Florida land to Capital.[5] If the estate were able to establish success-

[3] This litigation was initially instituted in 1963 by Capital to quiet title to the Virginia property. The issues we decide today arise by way of counter-claim filed by Morrison in 1965.

[4] Note No. 1, for $25,000, was paid by Do-Mor; Note No. 2, for $50,000., was sold to Mrs. Morrison and was subsequently paid by Frost and Dreisen. This appeal concerns the ownership of notes 3 and 4, for $100,000. and $225,000. respectively.

[5] The record is clear that default occurred on the notes issued by Capital as payment for the Virginia and Florida properties. Capital claims to have paid as much as $28,500; Morrison denies receiving more than about $4,000—both figures far from the purchase price in excess of one million dollars. This default forms one

[footnote continued]

fully that Morrison was entitled to such a constructive trust, the claim is that it would prevail over the interest of Frost and Dreisen in the notes or the Florida land itself.[6] This, they say, is because we held the last time this case was before us that Frost and Dreisen were not holders in due course of the Do-Mor notes under §3-306 of the Uniform Commercial Code, and hence took the notes from Capital subject to all valid claims on the notes against Capital. 484 F2d 1157 (4th Cir. 1973). In the last appeal we remanded to the district court to determine whether, as between Morrison, on the one hand, and Frost and Dreisen on the other, Morrison was entitled to a constructive trust in the two notes in question.[7]

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of the bases of Morrison's executors' claim of entitlement to a constructive trust on the ground of Capital's unjust enrichment. They also claim that the Florida land was conveyed without consideration because they say the agreement of July 29, 1963, applied only to the Virginia property and superceded the earlier agreement that undeniably pertained to both the Florida and Virginia lands.

Parenthetically, it should be noted the Morrisons foreclosed on a later obtained deed of trust they held on the Virginia property in 1970, which was sold for $700,000 to themselves. Morrison's executors obtained a deficiency judgment for about $400,000 against Capital in 1971.

[6] Following Do-Mor's default on notes 3 and 4, Frost and Dreisen foreclosed on the Florida property, and purchased it at the foreclosure sale. The notes having been satisfied in part, at least, from the proceeds of the sale, Morrison's executors apparently now claim either the property itself as standing in place of the notes, or the benefit of any deficiency still owing by Do-Mor.

[7] Our most recent decision in this case reversed the district court's 1972 judgment that denied a constructive trust on the basis of equitable principles of real estate law, favoring Frost and Dreisen as good faith purchasers without notice. We held that the case was controlled by the Uniform Commercial Code provisions dealing with the purchase of negotiable instruments.

[footnote continued]

On remand, the district court held that the estate failed to meet its burden of proof on the issue of a constructive trust. Specifically, it found that the 1.1 million dollar purchase price was consideration for both the Virginia and Florida properties, not for the Virginia property alone. The district court also held that it was necessary to prove fraud before a constructive trust should be imposed, and that the estate failed to meet its burden of proving fraud on the part of Benn, the owner of Capital. While Morrison concededly never received full payment on the notes issued by Capital for the purchase price, to the extent those notes were unsecured Morrison was merely a general creditor of Capital with claim for payment of the notes which has been prosecuted to a conclusion.

I.

The estate claims that the district court committed error in requiring proof of fraud to establish a constructive trust. It asserts that the constructive trust remedy can be administered with considerably more flexibility, specifically where unjust enrichment is demonstrated. The district court stated that "[t]he basis of a constructive trust is fraud, actual or constructive," citing cases, and imposed upon the appellant the burden of proving fraud by "clear and convincing evidence." *Sutton v. Sutton,* 194 Va. 179, 72 S.E.2d 275 (1952); *Malbon v. Davis,* 185 Va. 748, 40 S.E.2d 183 (1946).

There are statements in the Virginia cases, relied upon by the district court, suggesting that either fraud

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We also held that the district court's 1971 opinion, in which Morrison's executors prevailed in their constructive trust claim, was not controlling since Frost and Dreisen were not parties to the litigation at that time.

or breach of a fiduciary duty is requisite to the imposition of a constructive trust. *Miller v. International Union of Brewery Workers,* 187 Va. 889, 48 S.E.2d 252 (1948); *Porter v. Shaffer,* 147 Va. 921, 133 S.E. 614 (1926). While there is persuasive authority that unjust enrichment may constitute a ground for the creation of a constructive trust,[8] we find it unnecessary to express an opinion on the matter, for we hold that the district court was not clearly erroneous in finding that the sale of the Florida land was supported by valuable consideration. This compels the conclusion that, absent fraud, there was no unjust enrichment in this case as a matter of law sufficient to justify a constructive trust. There was at most a basis for a suit for damages, and this claim, if it ever existed, is co-extensive with the $400,000 judgment already obtained in 1971 against Capital by Morrison's estate and the Morrisons' foreclosure upon the purchase money notes.

The contract of May 18, 1963, pursuant to which Morrison agreed to convey the Florida property, recites a consideration for the conveyance of 1.1 million dollars, in the form of a judgment note payable within five years and bearing six percent interest.[9] As a matter of basic contract law, mutual promises constitute a valuable consideration in a bilateral contract. *Adams, Payne & Gleaves v. Indiana Wood Preserving Co.,* 155 Va. 18, 154 S.E. 558 (1930); *Bernstein v. Bord,* 146 Va. 670,

[8] See *Buchanan v. Brentwood Fed. Savings & Loan Ass'n,* 320 A.2d 117, 126-7 (Pa. 1974); *Annon v. Lucas,* 185 S.E. 2d 343, 352 (W. Va. 1971); D. Dobbs, *Handbook on the Law of Remedies,* §4.3 at 246 (1973); 4 Scott, *The Law of Trusts* §462 at 3103 (2d ed. 1956); 31 *Va. L. Rev.* 962 (1945).

[9] Morrison also took all of the capital stock of Capital in escrow as collateral to secure the payment of the purchase price.

132 S.E. 698, 699-700 (1926). That the notes executed and delivered by Capital for the payment of the purchase price to Morrison constituted a consideration for the conveyance and a legally binding obligation needs no further elaboration than reference to the Morrisons' foreclosure on those notes and the obtaining of a deficiency judgment by Morrison's estate.

Morrison's estate's argument that the July 29, 1963 contract superceded the earlier agreement and left the Florida conveyance unsupported by consideration is without merit. The district court, with all interested parties before it,[10] unequivocally found that the purchase price of the Virginia and Florida properties together was 1.1 million dollars, and that the July agreement reaffirmed the earlier agreement and conveyance. This finding, in the words of the district court, "is established beyond doubt." The district court's interpretation of the July transaction, that it was intended solely to secure Mrs. Morrison's necessary cooperation in fulfilling the obligations of the May contract, and not to displace that agreement, is amply supported by the record.

In order for Morrison's estate to rely upon the breach of an arms-length contract as the basis for a constructive trust it is necessary to prove that the breaching party never intended to perform his contractual obligations—a circumstance which may constitute fraud. It had the burden of proving fraud by clear and convincing evidence. *Malbon v. Davis,* 185 Va. 748, 40 S.E.2d 183, 187

[10] The district court's 1971 holding that the Appellants were entitled to a constructive trust was based on its finding, with opposing parties not before it, that the Florida conveyance was not supported by consideration. The finding was reconsidered by that court when both sides were in court and represented.

(1946). The district court found that "not a particle" of evidence had been presented by appellants to prove fraud since 1964, when Judge Butzner, sitting as a district judge in this case, came to the conclusion that neither the May, 1963 nor the July, 1963 contracts and conveyances were procured by actionable fraud.[11] Thus two district judges after full hearings in the protracted history of this litigation have rejected the contention that Capital committed fraud in its transactions with Morrison.

We have examined the allegations in appellants' brief intended to establish Benn's fraud (meaning Capital). We note that they consist largely of a list of unsavory activities from Benn's life over the past twenty years. It is not our province to pass judgment on Benn's life, only to review whether the district court's conclusion was clearly erroneous with respect to a particular sale of land in 1963. We conclude that it was not. Benn and Morrison testified orally before Judge Butzner who found no fraud. Judge Kellam found no evidence of it after Judge Butzner's finding. We do not think the findings are clearly erroneous. FRCP 52(a).

What we are left with, then, is a situation in which notes taken in consideration for the sale of land were not paid. The transaction was untainted by fraud and supported by a valuable consideration. Nothing prevented Morrison from taking a purchase money deed

[11] While Judge Butzner's finding of no fraud on the part of Capital, affirmed by this court in 360 F2d 462 (4th Cir. 1966), may be res judicata on that issue against those who were parties to that proceeding, or may work an estoppel in other situations, we do not find it necessary to rely on that principle nor similarly upon the result of a suit in Florida to which Morrison was a party which apparently held, after the conveyance to Capital, that he had no further interest in the Florida land.

of trust on the real estate as security for payment of the purchase price as he agreed to take the Capital stock as security. There is simply no theory under which a mere failure to pay a debt can justify the imposition of a constructive trust. *McKee v. Paradise*, 299 U.S. 119 (1936); *Cherno v. Dutch American Mercantile Corp.*, 353 F2d 147, 154 (2d Cir. 1965); see *Porter v. Shaffer*, 147 Va. 921, 133 S.E. 614 (1926). Were a contrary rule to prevail, its effect would often be to create an unwarranted preference in favor of one general creditor over others. *McKee*, p. 123.

II

As an alternate ground for its holding, the district court relied upon a release executed by Morrison on August 6, 1963, releasing Capital and Benn from all claims arising out of the sale of the Florida property. Appellants seek to avoid the effect of this release by arguing that it was unsupported by consideration, notwithstanding that it acknowledges receipt of valuable consideration and was executed under seal.

Under Virginia law, a sealed instrument generally conclusively imports consideration so far as the parties[12] to the agreement are concerned. *Norris v. Barbour*, 188 Va. 723, 51 S.E.2d 334 (1949); *Turner v. Hall*, 128 Va. 247, 108 S.E. 861 (1920); see *Northwestern Nat'l Ins. Co. v. Cohen*, 138 Va. 177, 121 S.E. 507, 508 (1924); *Ferries Co. v. Brown*, 121 Va. 13, 92 S.E. 813 (1917). While this rule does not necessarily obtain when the instrument is attached for fraud, and it is true that equity will look to the substance rather than the

[12] When a party has died, the rule may be relaxed. See e.g. *Norris* and *Cooper*, infra.

form of a transaction to prevent a fraud, see *Cooper v. Gregory*, 191 Va. 24, 60 S.E.2d 50 (1950), Morrison's executors, with the burden of producing evidence upon them failed to show that Capital obtained the release in a fraudulent manner, or indeed that the release was in any way irregular.[13] The district court's conclusion that the release was supported by valuable consideration is in accord with applicable law, is based on facts supported by the record, and is not clearly erroneous. FRCP 52(a).

We have considered the other assignments of error and find them to be without merit.

The judgment of the district court is accordingly

AFFIRMED.

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[13] The case of *Woody v. Schaaf*, 106 Va. 799, 56 S.E. 807 (1907), is very nearly indistinguishable on its facts from the case at hand. There, an obligation under seal given for an antecedent debt was in issue after the death of the maker of the obligation. The court held that, as against the maker's estate, the seal was conclusive evidence of the debt, and, as against an insurance company involved which was defending on the ground its policy on the maker's life was a wager policy, the seal was *prima facie* evidence.

Prima facie evidence, in Virginia, shifts the burden of going forward with the evidence. *Witt v. Merricks*, 210 Va. 70, 168 S.E. 2d 517 (1969). It is evidence which on its first appearance is sufficient to raise a presumption of fact or establish the fact in question unless rebutted. It imports that the evidence produces for the time being a certain result, but that the result may be repelled. *Babbitt v. Miller*, 192 Va. 372, 64 S.E.2d 718 (1951).

Here, applying the rule of *Woody* rigidly, the release under seal would conclusively establish consideration against Morrison's estate. But, assuming for argument that Morrison's estate had some kind of equity (which we do not decide) to place it in the position of those in *Norris* and *Cooper* who sought to avoid the effect of consideration imported by a seal, the instrument under seal nevertheless established *prima facie* evidence of consideration. The district court held that Morrison's estate had failed to prove there was no consideration, which furnishes an additional reason for its conclusion. Its finding is supported by the record.

APPENDIX E

IN THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

Civil Action No. 2968

CAPITAL INVESTORS CO.,
Plaintiff,

v.

ARTHUR R. MORRISON, et al.,
Defendants.

MEMORANDUM OPINION AND ORDER

In what it is hoped will be the final act in this long drawn out litigation, the Court is again called upon to decide issues growing out of the actions and conduct of Arthur R. Morrison (Morrison). The Court of Appeals for the Fourth Circuit in its opinion of September 12, 1973, reversed this Court's findings and remanded the case for further proceedings.

Following remand, the Court immediately notified counsel for each of the parties they would be given the opportunity to present such additional evidence and argument as they desired. Following a prescribed plan of procedure, counsel listed the exhibits they wished to use, designated the portions of the prior testimony relied on, listed witnesses, filed briefs, and argued the matter orally.

While the issue now before the Court may be stated in a few words, the determination of that issue relates to much of the history of this action. Although this action was instituted to quiet title to a parcel of land in Rosslyn, Virginia, it expanded to include numerous other issues.

In general, it grew out of marital differences between two of the principal parties, Mr. and Mrs. Morrison, and disputes over their property. Judge Butzner in his findings of December 17, 1964, referred to those marital difficulties and said that Morrison had pursued "a determination to get the property in his own hands and at the same time put Mrs. Morrison in a position by which he could effectively bring pressure to bear upon her for his own reasons."

Among the property owned by the Morrisions was a parcel situated in Brevard County, Florida. Morrison sought to acquire title to this property in his sole name and to deal with it as his. It was this dealing that brings about the issue now before the Court.

I

In presenting the issue now before the Court, counsel have filed extensive briefs and exhibits, and directed the Court's attention to many events of prior hearings. Only one live witness has been added, and that testimony was rather brief.

Inasmuch as counsel have dealt at great length on the prior facts, it will be necessary to set forth some of them as the basis for the conclusions reached. This litigation has been lengthy and burdensome. Five trial judges have dealt with various phases of the case. It has been to the Court of Appeals on four separate occasions.[1]

In Morrison's dealings with the Virginia and Florida properties, he entered into numerous contracts. It seems safe to say that his actions led to numerous legal difficulties. Whether his contracts were wise or unwise is not

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[1] See 360 F.2d 462; 387 F.2d 591; 453 F.2d 1365; and 484 F.2d 1157.

the issue. He was a man of considerable experience in dealing with real estate. Some of his business associates were not of the highest character. But, he was an adult, and the Court found in the companion case of *First National Bank of Washington v. Arthur R. Morrison,* Civil Action No. 4732, by opinion order of September 14, 1971, that he was mentally competent and responsible for his contracts.

II

In early 1963 Morrison had been and was having difficulty with his wife. He transferred the Florida and Virginia properties to other parties. He would thereafter disregard such a transfer and again contract and attempt to deal with the property as if it was still titled in his name. Conveyances of his property to others often ended in disputes.

Many of the facts concerning the Florida property are not in dispute. In 1962 Morrison entered into negotiations with Malcolm B. Devers, A. T. Rossetter and James H. Pruitt, to obtain a loan of $30,000.00 on the Florida property. Title to the property was conveyed to Devers and a loan obtained shortly. Thereafter Morrison sought to obtain an additonal loan of $30,000.00. He agreed to convey the Florida property to Rossetter and Pruitt for some $360,000.00, upon their paying $30,000.00 in cash, assuming the then existing mortgage of $30,000.00, and executing a purchase money mortgage for the balance of the purchase price. Dispute arose with Devers and Morrison sought the assistance of James T. Benn. He refused to complete the sale to Rossetter and Pruitt or to repay the $30,000.00 loan, or the $30,000.00 advanced as a part of the purchase price. A charter had been obtained for a corporation named Do-

Mor for use of Devers and Morrison. They did not use it, but consented for Rossetter and Pruitt to do so.

Morrison entered into agreement with Capital on May 18, 1963, for the sale of the Virginia and Florida properties and conveyed each of these parcels to Capital. On June 21, 1963, Capital conveyed the Florida property to Do-Mor. Do-Mor issued a purchase money mortgage to secure 4 notes aggregating $400,000.00.

On July 18, 1963, Do-Mor filed suit in the Florida courts to clear the title to said Florida property. Devers, Morrison and Mrs. Morrison, and others, were named as parties. Morrison filed an affidavit, Mrs. Morrison filed a cross-claim asserting she owned an undivided one-half interest, and that Morrison had not been the sole owner at the time he conveyed it to Capital. Decree was entered declaring the Morrisons had no interest.

On July 29, 1963, Morrison and his wife entered into a supplemental agreement with Capital. The result was that $1,000,000.00 was fixed as the amount due by Capital, one-half of which was to be paid to Morrison and one-half to Mrs. Morrison. On August 6, 1963, Morrison executed a release of Capital and Benn of all claims against the Florida property.[2]

Subsequently, on December 17, 1964, the Court found the conveyances by the Morrisons to Capital to be valid, and that they had not been obtained by fraud.

On January 20, 1965, Morrison instituted a suit in Florida against Do-Mor seeking to establish an equitable lien in his favor on the Florida property. This action was dismissed in July 1966 for failure to prosecute.

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[2]See finding of facts in the opinion of this Court of August 25, 1972, which set forth the terms of the release, and that it specifically released any and all sums due by Do-Mor.

On March 11, 1965, Peters & Company, nominee of Frost and Dreisen, purchased notes numbered 3 and 4 in the amount of $100,000.00 and $225,000.00, respectively, of the series of 4 notes issued by Do-Mor and secured by purchase money mortgage on the Florida property.

By order entered in this suit on June 29, 1965, the Court decreed that Capital held a fee simple title to the Rosslyn property, and that it must execute a trust thereon to secure the $1,000,000.00 in notes due Morrison. The trust was executed. This finding was affirmed by the Court of Appeals. See 360 F.2d 462, 466.

Thereafter, on September 9, 1966, Morrison filed another action in Florida against Do-Mor and others to enjoin Do-Mor from making payment of the notes of June 1963 to Capital or Benn.[3] After attempts by Dreisen and others to bring the suit to trial, Morrison took a voluntary nonsuit on February 12, 1971.

By the order of August 25, 1972, this Court held that Morrison had no interest in the Do-Mor notes or their proceeds. While this finding was pending on appeal to the Court of Appeals, the Court in Florida issued a Summary Judgment of Foreclosure of the mortgage to satisfy the Do-Mor notes. The property was sold at public auction and purchased by Dreisen and the Estate of Frost, who received a title therefor. They paid Mrs. Morrison note numbered 2 of some $79,000.00.

Thereafter the Court of Appeals reversed this Court's order of August 25, 1972, and remanded the action.

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[3]Note No. 2 of these 4 notes, in the sum of $50,000.00, was sold by Capital to Mrs. Morrison. The allegations in the Florida action and the relief sought are set forth in the Court's opinion of August 25, 1972.

In the remand the Court of Appeals said -

> The issuance of a constructive trust in the notes in favor of the estate accordingly remains for resolution between the estate and the defendants Frost and Dreisen. This cause is remanded to the District Court to make appropriate findings on that issue on the record heretofore made before it, supplemented by any additional evidence either party may submit. 484 F.2d 1163.

Further in the opinion the Court of Appeals noted a release had been executed by Morrison in favor of Capital. The Court said -

> So far as the release is concerned . . . it is the position of the estate that there was either a want or failure of consideration. While the District Court did not clearly rule on this contention of the estate, the fact that it did not predicate its conclusion on the release would suggest that it considered the position of the estate well taken. This issue is, however, tied in to the question of a constructive trust and may be reviewed on remand on the basis of the evidence adduced on that issue. 484 F.2d 1163.

The parties state that the issue before the Court is -

> Whether the Estate of Arthur R. Morrison is entitled to a constructive trust in the Do-Mor notes held by Frost and Dreisen or their proceeds.

III

Constructive trusts are those which the law creates under certain circumstances, independent of the intention of the parties, in order to prevent fraud or injustice which would otherwise ensue. They are trusts forced upon the parties by operation of law. Whenever title to property, real or personal, has been obtained through

misrepresentation or fraud, equity impresses a constructive trust on the property thus acquired in favor of one who is truly and equitably entitled to the same. *Porter v. Shaffer,* 147 Va. 921, 133 S.E. 614, 616; *Pair v. Hook,* 195 Va. 196, 77 S.E.2d 395; *Patterson's Exors. v. Patterson,* 144 Va. 113, 131 S.E. 217; *Carlton Min. & Power Co. v. West Virginia Northern R. Co.,* 113 W. Va. 20, 166 S.E. 536, cert. denied 289 U.S. 734; Michies Jur. Vol. 19 page 98 ¶ 48, subject Trusts and Trustees. The basis of a constructive trust is fraud, actual or constructive. *Sutton v. Sutton,* 194 Va. 179, 72 S.E.2d 275, 278; *Malbon v. Davis,* 185 Va. 748, 40 S.E.2d 183, 187; *Porter v. Shaffer, supra* [133 S.E. 616]; *Sweeny v. Patton,* 134 Va. 117, 113 S.E. 715, 716; Michies Jur. Vol. 19 pages 98 and 99, ¶ 48, subject, Trusts and Trustees. As the Court said in *Wilson v. Wall,* 73 U.S. (6 Wall.) 83, 91 -

> A chancellor will not be astute to charge a constructive trust upon one who has acted honestly and paid a full and fair consideration without notice or knowledge. On this point we need only to refer to Sugden on Vendors, where he says: "In *Ware v. Lord Egmont* the Lord Chancellor Cranworth expressed his entire concurrence in what, on many occasions of late years, had fallen from judges of great eminence on the subject of constructive notice, namely, that it was highly inexpedient for courts of equity to extend the doctrine. When a person has not actual notice he ought not be treated as if he had notice unless the circumstances are such as enable the court to say, not only that he *might have acquired,* but also that he ought to have acquired it but for his gross negligence in the conduct of the business in question. The question then, when it is sought to affect a purchaser with constructive notice is not whether he had the means of obtaining and

might by prudent caution have obtained the knowledge in question, but whether not obtaining was an act of gross or culpable negligence."

The above language is particularly applicable here, for Frost and Dreisen acted honestly and paid a full and fair consideration, without notice or knowledge of any claim or interest or right of Morrison.

Fraud is a serious charge; it must be alleged; it is never presumed; and it must be established by clear and convincing evidence. Fraud is an artifice employed by one person to deceive another. *United States v. Wunderlich,* 342 U.S. 98, 100; *United States v. Colorado Anthracite Co.*, 225 U.S. 219, 226 (1912); *Kuhn v. Chesapeake and Ohio Railroad Co.*, 118 F.2d 400 (4th Cir. 1941); *American Insurance Co. v. Lester*, 233 F.2d 291 (4th Cir.1956); *Krodel v. Houghtaling,* 427 F.2d 159 (4th Cir. 1970); *Merrill-Stevens Dry Dock Co. v. M/V Laissez Faire*, 421 F.2d 430 (5th Cir. 1970 Fla.) *Lucom v. Atlantic National Bank, etc.*, 354 F.2d 51 (5th Cir. 1965 Fla.), cert. denied 385 U.S. 898; *Ramey v. Koons,* 230 F.2d 802 (5th Cir. 1956 Fla.); *Gibson v. Gibson,* 207 Va. 821, 153 S.E.2d 189; *Reiber v. James M. Duncan, Jr. & Assoc.*, 206 Va. 657, 145 S.E.2d 157; *Malbon v. Davis, supra.* In *Malbon v. Davis,* the Court quoted with approval the following from *Redwood v. Rogers,* 105 Va. 155, 158, 53 S.E. 6,7:

"The charge of fraud is one easily made, and the burden is upon the party alleging it to establish its existence, not by doubtful and inconclusive evidence, but clearly and conclusively. Fraud cannot be presumed. It must be proved by clear and satisfactory evidence. It is true that fraud need not be proved by positive and direct evidence, but may be established by facts and circumstances sufficient to support the conclusion of fraud. But whether it be shown by direct and positive evidence, or established by circumstances, the proof must be clear and convincing, and such as to satisfy the conscience of the chancellor, who should be cautious not to lend too ready an ear to the charge."

This principle has been reaffirmed in numerous cases. *Haynes v. Peterson,* 125 Va. 730, 733, 100 S. E. 471, 6 A.L.R. 1456; *Barbour v. Barbour,* 155 Va. 650, 156 S.E. 365; *McClintock v. Royall,* 173 Va. 408, 4 S.E.2d 369.

And so to establish a constructive trust in this case the burden rests upon the Morrison Estate to prove its case "by evidence which is clear, definite and convincing." *Sutton v. Sutton, supra* [72 S.E.2d 278]; *Malbon v. Davis, supra* [40 S.E.2d 183]; *Zogg v. Hedges*, 126 W.Va. 523, 29 S.E.2d 871, 874, 152 A.L.R. 991. This the Estate has failed to do, as we shall hereafter see.

IV

We turn then to the evidence in this case, to determine whether it meets the test. The Court finds from the evidence presented -

(1) Morrison and his wife had been divorced. He was attempting to secure complete control of certain property, beyond any claim of his wife.

(2) In attempting to remove the Florida property from any control of his wife, he conveyed title to Devers. Devers obtained a loan of $30,000.00 for Morrison. Needing further funds, Morrison agreed to convey the property to Rossetter and Pruitt, from which he obtained another $30,000.00, and was to receive a note for $360,000.00.

(3) Morrison became displeased with Devers and Rossetter and Pruitt, and entered into an

agreement with Capital Investors Co. (James T. Benn), on May 18, 1963. This agreement set forth that Morrison "hereby sells, conveys, transfers, assigns and delivers" unto Capital, the Rosslyn and Florida properties, and "all monies due and to become due from James A. Pruitt and A. T. Rossetter and Do-Mor . . ." relating to property in Brevard County, Florida. The agreement further sets forth that the properties were conveyed to Capital under separate appropriate documents dated May 18, 1963, that seller irrevocably accepts from buyer $1,100,000.00 in a judgment note payable 5 years from date with interest at 6%; that the capital stock of Capital Investors would be placed in escrow until the note was paid; that seller on or about June 28, and September 4, 1962, sold the Florida property to Pruitt and Rossetter, but that Morrison by said agreement transferred his interest to Capital; and that no agreements, representations, understandings, etc. not included in the agreement would be binding or have any effect.

(4) By deed of May 18, 1963, Morrison conveyed the Florida and Virginia properties to Capital. By deed of June 21, 1963, Capital conveyed the Florida property to Do-Mor, which in turn executed a mortgage to secure $400,000.00 and agreed to release trusts of $60,000.00.

(5) On June 21, 1963, Capital assigned notes Nos. 3 and 4 of the Do-Mor mortgage to Brevard Properties, Inc., and Brevard on the same day assigned them to Southgate Associates, Inc.

(6) By agreement of March 16, 1965, Southgate Associates assigned said notes and mortgage to Peters & Company, nominee of Frost. On August 9, 1965, Peters & Company assigned the notes and mortgage to Harry Dreisen.

(7) A suit was filed in Florida by Do-Mor to clear the title to the Florida property. Subsequently, action was filed by Morrison in September 1966, to assert a claim to said notes. This suit was dismissed February 1, 1971 for failure to prosecute. These actions were dealt with in detail in the prior Memorandum Opinion of this Court.

Hence, Morrison by the agreement of May 18, 1963, agreed to and did convey to Capital all his interest in the Virginia and Florida properties and specifically set forth the conveyance included "all monies due and to become due from James A. Pruitt and A.T. Rossetter and Do-Mor Development" relating to the Florida property. The agreement set forth that Morrison irrevocably accepted from the buyer a judgment note payable 5 years after date and an agreement to place the stock of Capital in escrow until the note was paid. The agreement was confirmed by Morrison by execution of deeds conveying the properties. The judgment note was delivered and the stock placed in escrow.

On June 21, 1963, Capital conveyed the Florida property to Do-Mor in exchange for a mortgage securing $400,000.00.[4] The notes numbered 3 and 4 of this mortgage, for $100,000.00 and $225,000.00, respectively, are the subject of the present issue before the Court. On that same day Capital assigned these two notes to

[4]Note No. 1 for $25,000.00 was paid; Note No. 2 for $50,000.00 was sold to Marian Morrison.

Brevard Properties, and the same day Brevard assigned them to Southgate Associates. On March 16, 1965, Southgate Associates assigned the notes in question to Peters & Company, which on August 9th assigned them to Dreisen. Peters & Company was the nominee of Frost. These various assignments were duly recorded in the records in Florida.

In the agreements of sale Morrison was required to clear the titles to the Virginia and Florida properties.

In his efforts to outdo his wife, Morrison had complicated the titles to the real properties. The title to the Virginia property was almost hopelessly involved, and Mrs. Morrison's cooperation was necessary. By agreement of July 23, 1963, Mrs. Morrison agreed to cooperate. In that agreement she set forth that on June 15, 1963, she had been informed by her husband that he had sold all his interest in the Virginia and Florida properties. By agreement of July 29, 1963, Morrison affirmed the agreement and conveyances of May 18th, and his undertaking to clear the titles to said properties, in exchange for a promissory note of $1,100,000.00. The agreement further set forth Morrison could not perform his contract, and that he could not deliver a clear title because of claims of Mrs. Morrison; that because of his inability to perform, he agreed to surrender $500,000.00 of the $1,100,000.00 in notes to be delivered to Marian A. Morrison for her interest in the property. At that time, this action instituted by Capital was pending in this Court. Mrs. Morrison agreed to intervene in this suit; she ratified and affirmed all agreements theretofore made between Capital and Morrison, and that the total of all indebtednesses from Capital for all of its purchases and dealings should not exceed $1,000,000.00, and the cost of clearing title would not exceed $100,000.00.

When this agreement was signed by the parties ratifying all of the other contracts and agreements and fixing the total of all sums due by Capital to the Morrisons at $1,000,000.00, this action by Capital to clear the title to the Virginia property was pending. Capital held a warranty deed for the Virginia and Florida properties. Capital had sold and conveyed the Florida property, and had assigned the two notes of Do-Mor now in issue.

In this suit instituted by Capital to quiet title, Devers asserted various claims, as did others. The issue of the sufficiency of the notes given by Capital and accepted by Morrisons arose, as did numerous other issues. On December 17, 1964, Judge Butzner found that the Morrisons conveyed the Virginia property to Capital and that the deed was not procured by actionable fraud. He directed security in the form of a deed of trust be given for the sums due. While the Court there referred to some indebtedness arising out of the Florida property, it did not deal with the purchase price or notes in question. It is established beyond doubt that the total purchase price of the Virginia and Florida properties was $1,000,000.00 plus $100,000.00 for costs to clear the titles. This is clearly set forth in the agreement of May 18, 1963, the agreement of July 23, 1963, the agreement of July 29, 1963, the stamps affixed to the recorded deeds, the complaint filed by Morrison in the suit instituted by him in Florida on September 8, 1966, in the counter-claim filed by Morrison in this suit (C/A 2968) of February 1, 1965, the revised counter-claim of October 24, 1966, filed in this action, the testimony of Morrison set out in Frost and Dreisen Exhibits 69, 73 and 75, and the agreement of July 25, 1974 between the Executors of Morrison and Mrs. Morrison.

In the counter-claim of February 1, 1965, Morrison set forth that by the agreement of May 18, 1963, he had agreed to convey all his "interest in and to properties in Brevard County, Florida, monies due from sale of said properties in Florida" and that he had delivered a good conveyance for same; that Capital had agreed to place its stock in escrow and pay the purchase price as legal title was cleared; that Capital had converted the Florida properties into cash or its equivalent of approximately $400,000.00, but failed to apply said funds to the notes due him. He further alleged that Capital had "already pledged the proceeds of the Florida lands as security for other corporate borrowing and sold one of the notes to co-defendant, Marian Morrison."

We have a situation where Morrison sold and conveyed property accepting unsecured notes for the purchase price. Security in the form of a deed of trust on the Virginia property was later obtained. Had Capital paid the $1,000,000.00 worth of notes, Morrison would have no sum due and therefore could not possibly assert a claim by constructive trust, or otherwise, in the Do-Mor notes or their proceeds.

Of course, while Capital still held the Do-Mor notes, in a proper proceeding Morrison might attach the notes or their proceeds, upon a proper showing that Capital was attempting to dispose of such assets to defraud its creditors. But no such action was instituted or pending while Capital had possession or control of the notes, or prior to the time they had been sold to Frost and Dreisen. In March 1965, when Frost purchased the notes made by Do-Mor, Morrison had no lien, equitable or otherwise, and had no claim to the notes. Because Morrison had a debt due from Capital did not entitle him to a lien on the notes or the proceeds, without more. Actually, Capital acquired and possessed the notes by and with the consent and agreement of Morrison. Even if Morrison would be entitled to relief because of any fraud, he has failed to prove fraud.

Whether it was good business for Morrison to contract as he did, or to deal with Capital as he did, is not the issue. The Court would be quick to say one should not part with the title and possession of real property without retaining a lien for the purchase price; that the assignment of Capital stock, a closely held corporation with few or no assets as security for a debt due, was little or no security, particularly unless the escrow agent controlled all voting power and actions of the corporation. But Morrison, for his own reasons and purposes, entered into these agreements, He was an adult, experienced in dealing with real property, and had been rather successful.

In *Malbon v. Davis, supra,* the Court quoted with approval the following from *Hancock v. Anderson,* 160 Va. 225, 168 S.E. 458, 464:

> "The presumption is that people who deal with each other, grown men and women, deal with each other as such, and this presumption is not destroyed by disparity in age nor by the ties of blood, and this is particularly true where fraud is charged, either actual or constructive. Moore v. Gregory, 146 Va. 504, 131 S.E. 692."

In *International Refuge Organization v. Maryland Drydock Co.,* 179 F.2d 284 (4th Cir. 1950), Chief Judge Parker, writing for the Court, said at page 287:

> The fact that a court of equity will decree a constructive trust in property obatined by fraud or purchased with funds obtained by fraud does not mean that the title of the owner is defective or his posses-

sion tortious. A constructive trust is not a title to or lien upon property but a mere remedy to which equity resorts in granting relief against fraud; and it does not exist so as to affect the property held by a wrongdoer until it is declared by a court of equity as a means of affording relief. See Pomeroy's Equity Jurisprudence 4th ed. vol. 3, sec. 1044, pp. 2371-3; A.L.I. Restatement of Restitution sec. 160; 54 Am.Jur. pp. 169-170; Rolfe v. Gregory, 4 De Gex, J. & S. 576, 579; In re Farmers State Bank, 67 S.D. 51, 289 N.W. 75, 126 A.L.R. 619; Edwards v. Culbertson, 111 N.C. 342, 16 S.E. 233, 234, 18 L.R.A. 204. As said in the case last cited: "The trusts of which we are speaking are not what is known as 'technical trusts,' and the ground of relief in such cases is, strictly speaking, fraud, and not trust. Equity declares the trust in order that it may lay its hand upon the thing and wrest it from the possession of the wrongdoer."

Any claim which IRO had arising out of the fraud of Madeiros was of a personal nature, not constituting a lien upon or claim against the vessel and not affecting the rights of the owner to use her for purposes of commerce or to enter into obligations with that in view. There can be no question but that claims for repairs made under a contract with the owner would take precedence over any such equitable claim.

In *Cherno v. Dutch American Mercantile Corp.*, 353 F.2d 147, 154 (2d Cir. 1965), the Court in dealing with the issue of a constructive trust allegedly growing out of the breach of agreement said:

> Blanmill breached that agreement, but breach of a contract concerning payment of a debt furnishes no basis for the finding of a constructive trust. Bogert, Trusts & Trustees §479 at 89 (2d ed. 1960)

See also Amerada Petroleum Corp. v. Burline, 231 F.2d 862 (10th Cir. 1956).

Morrisons have failed to establish that a constructive trust existed at any time before the Do-Mor notes were sold and assigned; or that the notes were ever held by anyone as the proceeds of a constructive trust. Granted, it was poor business judgment for Morrisons to convey the property in exchange for unsecured notes, but poor business judgment does not establish a constructive trust.

I find no credible evidence in the record to show that Frost and Dreisen were a party to any improper dealings of Capital or Benn or any of their associates. There was nothing of record to show anyone other than Capital and its assignees had any claim to the notes of Do-Mor. We are not here concerned with whether the makers of the notes might have a good defense to the debt due, but whether a party in possession, who has purchased the notes without any knowledge or notice of any claim of another in the nature of a constructive trust, may hold them. There is no credible evidence, or inference, which establishes Frost and Dreisen had any knowledge or notice of any claim of Morrison to the Do-Mor notes at the time of their purchase.

Not only did Judge Butzner not find actionable fraud on the part of Capital, but he confirmed the contracts between Capital and the Morrisons. At that time the Do-Mor notes were already owned by Frost and Dreisen. Not until September 1966 did Morrison institute action to claim any ownership or interest in the Do-Mor notes. This suit he dismissed February 1971 without prosecuting it. It was after such dismissal that he brought Frost and Dreisen into this suit.

Since Judge Butzner's finding of no actionable fraud on the part of Capital, which was affirmed by the Court of Appeals, not a particle of evidence has been presented to establish any such fraud. Without it, Morrisons cannot recover herein.

Frost and Dreisen were bona fide purchasers for value and in good faith, and had no actual or constructive notice of any claim by Morrison to the notes or of any breach of trust in the transfer of the notes. Morrison's remedies are against Capital and Benn. Vol. 54 Am. Jur. page 209, ¶ 266, subject Trusts; Vol. 19 Michies Jur. page 130, ¶ 68, subject Trusts and Trustees.

V

In view of the findings of the Court it does not seem necessary for the Court to deal with the issue of the effect of the release executed by Mr. Morrison on August 6, 1963. While the Court's ruling on the above issue, if sustained by the Court, will dispose of this case, if the Court of Appeals should differ with that finding, then the issue of the general release may become relevant. With the hope of having a final determination of all issues in this case, I proceed to the question of whether "there was either a want or failure of consideration," [484 F.2d 1163] for the release.

The general release is dated August 6, 1963, signed by Arthur R. Morrison, witnessed by two witnesses, and acknowledged before a Notary Public. The language of the release is adequate for the purposes for which it is offered. After general language of release, it specifically releases all claims arising out of the dealings with the Florida property "including any and all monies due or to become due from Do-Mor . . . Pruitt and his wife. . . ."

But here, the release states a consideration; it is under seal which purports a consideration. The burden is therefore upon Morrison to show there was no consideration. Not a particle of evidence has been presented on this issue. *Norris v. Barbour,* 188 Va. 723, 51 S.E.2d 334, 339 (1949); *Mitchell v. Wayave,* 185 Va. 679, 40 S.E.2d 284; *Watkins v. Robertson,* 105 Va. 269, 54 S.E. 33. True, on proof of fraud, valuable consideration may be shown. But there is no evidence of fraud in the obtaining of the release.

The release is therefore valid and binding.

At time of execution of the release by Morrison, he had already conveyed the Virginia and Florida properties to Capital by warranty deeds, and contracted to clear the titles. $100,000.00 of the purchase price of $1,100,000.00 was described as the sum to be used for this purpose. In the agreement of July 29, 1963, Morrison recited he was unable to deliver the title contracted for. Notes for the $1,100,000.00 had been delivered to Morrison. He had lost or misplaced some of them. There were numerous other dealings between Morrison and Capital. The May 1963 agreement referred to certain property pledged to First National Bank of Washington. The conveyance by Morrison of the Florida property had failed to set forth that the conveyance was subject to liens of $60,000.00. There were potential claims by Capital for breach of warranty. Mrs. Morrison was taking steps to acquire the fee simple title to the Virginia property. Had she been successful, Capital might have gone against Morrison for breach of warranty and a breach of contract.

Looking at the matter in retrospect, we would probably say that the dealings required mutual releases.

Capital and Benn had advanced Mr. Morrison various sums of money which Morrison said were for "Expenses and emergency needs" [Ptf. Ex. 10, testimony of Mr. Morrison September 1964]. Morrison said the advances were in cash.

Looking at the matter in retrospect, we would say that the dealings required mutual releases. It does not appear mutual releases were executed.

Even so, there was a valuable consideration for the release.

VI

In summary, Morrison contracted to and did sell and convey real and personal property, accepting unsecured notes therefor. The conveyance of the real estate was without recorded limitation against the sale and conveyance thereof. The purchaser sold and conveyed the real estate, accepting a purchase money mortgage for deferred payments. These notes were sold and assigned to a bona fide purchaser for value, without any notice of any claim of Morrison.

Morrison thereafter sought to establish a constructive trust against the real property and the proceeds of sale, i.e., the mortgage. To establish such a claim, he was required to prove fraud. The evidence presented did not meet the test of proving fraud and establishing a constructive trust. But, even if Morrison was entitled to relief against Capital and Benn, the evidence fails to show that at the time Frost and Dreisen purchased the notes in question, they had knowledge, either actual or constructive, of any claim of Morrison.

Having failed to carry his burden, the claim of Morrison is denied.

/s/ [Signature]
United States District Judge

Norfolk, Virginia
February 3rd, 1975.

APPENDIX F

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 73-1046

CAPITAL INVESTORS CO., and
NORMAN B. FROST and HARRY DREISEN,
Appellees,

v.

EXECUTORS OF THE ESTATE OF
ARTHUR R. MORRISON,
Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA,
AT ALEXANDRIA

Richard B. Kellam, District Judge

Argued May 8, 1973 Decided September 12, 1973

Before BOREMAN, Senior Circuit Judge, RUSSELL and FIELD, Circuit Judges

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Joseph B. Hyman (Echols and Hyman on brief) for Appellant

John A. Beck for Appellees Frost and Dreisen

RUSSELL, CIRCUIT JUDGE:

This is still another chapter in what has proved to be extended and protracted litigation arising out of a husband's unfortunate manipulation of his property in an apparent attempt to thwart his wife and representing

efforts either of him or his estate to reclaim his property from the consequences of his own manipulations. The property involved consisted of two valuable tracts of real estate. One was located in Virginia, the other in Florida. The early stages of the proceedings related to the Virginia property. The background of that phase of the litigation, as well as the general nature of the proceedings and of Morrison's efforts in concealment have already been detailed in earlier opinions of this Court and need not be repeated again.[1] At this time, we are only concerned with the Florida property.

In May, 1963, Morrison,[2] the husband, acting in conjunction with the defendant James T. Benn, deeded his Florida property to Capital Investors Co. (hereinafter described as Capital) which was a corporate "shell," owned and controlled completely by Benn, and which may be considered legally as identical with Benn. Capital promptly sold the property in June, 1963, to Do-Mor, Inc., a Florida corporation, which in payment executed four promissory notes of even date with the purchase, naming Capital as original payee. The notes were secured by a mortgage over the real estate sold. The controversy between the parties relates to only two of these notes, one in the principal amount of $100,000 payable in two equal installments on June 21, 1964, and June 21, 1965, and the second in the sum of $225,000, payable within sixty days, or August 21, 1963. After delivery, the notes were shifted about by Benn among three corporations, which represented his *alter egos* and were completely under his control and ownership. It is unnecessary to detail such manipulations since they have no determinative bearing on the issues in this phase of the litigation. In

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[1] 360 F.2d 462 (1966); 387 F.2d 591 (1967); and 453 F.2d 1365 (1972).

[2] Morrison died in 1969 and his executors were properly substituted in his place.

March, 1965, however, when both notes were in default and after maturity,[3] Benn, through one of his "shell" corporations endorsed the two notes in question to the defendant Frost, who initially had the notes endorsed over to a nominee, Peters and Company, a real estate brokerage firm headed by Frost's son-in-law, and later in favor of the defendant Dreisen, as nominee. Dreisen, however, later acquired from Frost a half-interest in his purchase. In December, 1964, prior to the negotiation of the notes to Frost, the District Court had directed that the proceedings should focus on the ownership of the Florida property, or, if sold, its proceeds, and directed that the parties should file specific statements of their claims in and to the property or its proceeds. In accordance with this judicial direction, Morrison submitted in February, 1965, motion for leave to file his counterclaim against Capital and Benn for the purpose of establishing his claim to the Florida property or, if sold, to the proceeds therefrom. This motion was granted in March, 1965, a few days after Benn had assigned the notes to Frost. Thereafter, Benn's corporate "shell," which had made the transfer of the notes to Frost's nominee, filed bankruptcy proceedings, listing these notes as corporate assets "subject to a pledge."

Little progress was made in disposing of the issues surrounding the ownership of the Florida property. The proceedings, it seems, were shifted about among judges after the District Judge who originally was in control was elevated to the Circuit Court. In December, 1970, however, Honorable Richard Kellam, District Judge, to

[3]Only the first installment on the $100,000 was past due but the Uniform Commercial Code declares that a "purchaser has notice that an instrument is overdue if he has reason to know (a) that any part of the principal amount is overdue * * *." Section 3-304(3). This seems to have been the rule under the NIL. Note, 170 A.L.R. 1029; *United States v. Capen* (D.C. Vt. 1944), 55 F.Supp. 81.

whom the case was ultimately assigned, began to press vigorously the proceedings towards a conclusion. He accordingly, in December, 1970 fixed a hearing to dispose of all outstanding issues, including particularly that involving the Florida property. Notice of this hearing and of the right of any party to proffer any claims he might have to this property was given all parties. After a full hearing in March, 1971, pursuant to the notice, the Court issued its opinion, dated May 4, 1971 in which it found specifically that Capital had not "paid any consideration for the Florida properties" and that Capital "held the assets described, transferred and conveyed as a constructive or resulting trustee. All of the properties were owned by Mr. Morrison. No consideration was paid by Capital. Mr. Morrison is entitled to have all of the property returned to him, or the proceeds therefrom, subject to the right of any bona fide transferee." In this opinion, it described the notes as "subject to a pledge," thereby indicating uncertainty of the nature of any claim of Frost and Dreisen, who were not at the time parties to the action, in and to the notes. This finding was confirmed in the judgment of the Court dated June 21, 1971.

Thereafter, the present controversy over the ownership of the two notes in question quickly developed between the estate of Morrison, relying on the judgment giving it beneficial equitable ownership of the Florida property "or the proceeds therefrom," and Frost and Dreisen claiming as endorsees and transferees for value without notice of the claims of Morrison. After a hearing on the respective claims, the District Court filed its decree "in equity" concluding, on the basis of its balancing of the equities of the parties, that the rights of Frost as a purchaser for value without notice were superior to those of the estate, even though the estate be deemed to have a constructive trust in and to the notes. Predicated on those findings, it sustained the claim of the defendants

Frost and Dreisen to the notes. In so ruling, the Court gave no consideration in its opinion to the Uniform Commercial Code and its applicability to the issues between the parties. The estate has appealed. We reverse.

The notes in dispute are negotiable instruments and the transferability of such notes, as well as the rights flowing from such transfers, are to be determined by the legal principles unique to negotiable instruments. This is so, though the notes are secured by a real estate mortgage.[4] In ascertaining what the rights attaching to a negotiation of a negotiable instrument are, the Courts are to apply the law, not of the place of payment, but of the place where the negotiation occurred.[5] The transfer of

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[4] This is made crystal clear in the Uniform Commercial Code. *See* Sections 3-105(2)(a) and 3-112(b) of the Code. 11 Am. Juris. 2d Section 201, at 230, summarizes the rule under the Code thus:

> "* * * The Commercial Code declares the negotiability is not affected by a statement that collateral has been given to secure obligations, either on the instrument or otherwise, of an obligor on the instrument, and an order or promise is not made conditional by the fact that the instrument states that it is secured."

This rule was the majority rule even before the adoption of the Code. *Marine Bank v. Kalt-Zimmers Co.* (1934), 293 U.S. 357, 363; *Gerrish v. Atlantic Ice & Coal Co.* (5th Cir. 1935), 80 F.2d 648, 650; *Fidelity Trust Co. v. Mayhugh* (5th Cir. 1920), 268 F. 712, 716-7; *First National Bank v. Valentine* (1970), 309 N.Y.S.2d 563.

[5] *U.S. v. Guaranty Trust Co.* (1934), 293 U.S. 340, 345-6; *Queensboro Nat. Bank of City of New York v. Kelly* (2d Cir. 1931), 48 F.2d 574, 576; Restatement, Conflict of Laws 2d, Sec. 216. In *Guaranty Trust*, the Court said:

> "But under settled principles of conflict of laws, adopted by both federal and state courts, the validity of a transfer of a chattel brought into a country by the consent of the owner is governed by its law; and that rule applies to negotiable instruments." (293 U.S. at 345-6.)

the notes in question to Frost occurred in the City of Washington. At the time of that transfer, the applicable law was represented by the Uniform Commercial Code, earlier adopted in that jurisdiction. All of this the defendants Frost and Dreisen conceded on oral argument. Nor could they have taken any other position in view of the clarity of the law. The District Court, in its decision from which this appeal is taken, however, gave no consideration to the provisions of the Uniform Commercial Code and erroneously applied general equitable principles applicable to the transfers of non-negotiable instruments in resolving the rights of the parties.

Broadly speaking, the Uniform Commercial Code divides the purchasers of negotiable paper into two categories; and, following the ancient maxim, *nomen est numen*,[6] it fixes the rights of a purchaser by his classification within those categories. The two categories are "holder in due course" and one not a "holder in due course." And the Code provides a simple test for ascertaining within which category a purchaser of a negotiable paper falls. To be a "holder in due course," one must have acquired the negotiable instrument before maturity and before default.[7] It is conceded that Frost acquired

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[6] Freely translated, this maxim is to the effect that "to name is to know or to decide."

[7] Sec. 3-302(c), U.C.C.

The reason for this differentiation between rights acquired by one under an assignment before maturity and one after maturity was long recognized before the adoption of either the Negotiable Instruments Act or the Uniform Commercial Code. " 'Where a negotiable note is found in circulation *after it is due, it carries suspicion on the face of it.* * * *' " (Emphasis in text.) *Osborn v. McClelland* (1885), 43 Ohio St. 284, 1 N.E. 644, 651, quoting from 1 Daniel, Neg. Inst. (1st Ed.), § 782. A like idea was expressed in *Vermilye & Co. v. Adams Express Company* (1874), 88

[footnote continued]

the notes in this case after maturity and with knowledge of default. It follows necessarily, then, that he was not a "holder in due course." The Uniform Commercial Code plainly provides that one not a "holder in due course," such as was Frost, takes the notes "subject to (a) all valid claims to it on the part of any person; * * *."[8] And the breadth of the phrase in the Code of "all valid claims * * * on the part of any person" is stated in the Official Comment on the section to include "not only claims of legal title, but all liens, equities or other claims of right against the instrument or its proceeds. It includes claims to rescind a prior negotiation and to recover the instrument or its proceeds." The Official Comment goes further and states that this provision "includes all claims for rescission of a negotiation, whether based in incapacity, fraud, duress, mistake, illegality, breach of trust or duty or any other reason. * * * It includes claims of legal title, lien, constructive trust or other equity against the instrument or its proceeds." The Comment, also, makes clear that the provision applies to and limits the rights of "a bona fide purchaser" for value, provided he

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U.S. 138, 144-5, where the Court said that the past-due character of a negotiable instrument "should be a warning to the purchaser of such an obligation after its maturity to look to the source from which it comes, and to be cautious in paying his money for it."

See, also, Morgan v. United States (1884), 113 U.S. 476, 500:

"When transferred after it has become due, although not reduced to the rank of an ordinary chose in action, the legal title to which cannot pass by assignment or delivery, it carries on its face the presumption which discredits it, and deprives it of that immunity which, while the time for payment was still running, was secured to it in favor of a bona fide purchaser for value without actual notice of any defect, either in the obligation or the title."

[8]Section 3-306, U.C.C.

took "with notice that the instrument is overdue."[9] Since Frost took the notes with actual notice they were overdue and in default, he acquired only the right of his transferor, Benn, in and to the notes or their proceeds and his right to the notes was specifically subject to any constructive trust in and to the notes or their proceeds

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[9]Section 3-306(a), U.C.C.; 11 Am. Jur. § 486, at 550.

The Code made little real change in the rights of one not a holder in due course under the old law merchant, which was to the effect that one not a holder in due course got by transfer only such title as his transferor had and, if some other person had legal or equitable title, such title would not be divested by the transfer. *Morgan v. United States, supra*, at 491 (113 U.S.); *Vermilye & Co. v. Adams Express Company, supra*, at 146-7 (88 U.S.); *Texas v. White* (1868), 74 U.S. 700, 735. In the latter case, the Court said:

"* * * We held in that case that the purchaser of coupon bonds, before due, without notice and in good faith, is unaffected by want of title in the seller, and that the burden of proof in respect to notice and want of good faith, is on the claimant of the bonds as against the purchaser.

* * *

"But these rules have never been applied to matured obligations. Purchasers of notes or bonds past due take nothing but the actual right and title of the vendors."

In *Morgan v. United States, supra*, the Court said (at 491, 113 U.S.):

"Purchasers of notes or bonds past due take nothing but the actual right and title of the vendors."

See, also, 11 Am. Jur. 2d § 481 at 541-2:

"A holder who takes an instrument after its maturity has, under the NIL or law merchant, "the status and rights, in general, of the holder of a non-negotiable instrument or of the assignee of a chose in action. That is, unless he holds through a holder in due course, he normally has nothing but the right and title of his transferor, is put upon inquiry and is chargeable with notice, and holds the instrument subject to defenses based on infirmities in the instrument or defects in title of the person transferring it to him."

in favor of the estate and all references in the District Court's opinion to the rights of a "bona fide purchaser" for value were irrelevant. In short, the controversy between the parties resolved itself into the clear-cut question whether the estate had established its right to claim the notes as the beneficiary of a constructive trust in the notes or their proceeds. If it had, Section 3-306 was applicable and controlling.

In its May 4, 1971 opinion, the District Court found that the estate did have a constructive trust in the notes or their proceeds. The estate asserts this finding in the May opinion is conclusive on the rights of the parties and on the existence of a constructive trust in its favor. But Frost and Dreisen were not parties to the proceeding at the time this opinion was rendered and they claim they are not bound by that decree. The estate counters with the argument that the May finding binds both parties and those in privity with them, and one is in privity if, though not a party, he acquired his interest in the subject-matter of the controversy after the commencement of the action thereon. In amplification of this point, it argues that Frost's purchase of the notes was after the proceeding was begun, after the District Court in its ruling of December, 1964 had focused on the Florida transaction, and after the estate had filed its motion to raise by counterclaim its claim to the property or its proceeds. There is, it may be conceded, considerable authority in support of this contention of the estate. *See Lamb v. Cramer* (1932), 285 U.S. 217, 219; *National Lead Co. v. Nulsen* (8th Cir. 1942), 131 F.2d 51, 56, *cert. denied*, 318 U.S. 758, 46 Am. Jur. 2d, Sec. 532 at 684; 1st Restatement of Judgments (1942), Section 89. But, under the special circumstances of this case, we do not regard the principle urged by the estate applicable. This is so, because the

District Court in its May, 1971 opinion, though finding favorably to a constructive trust, limited that finding to the parties then before the Court and expressly reserved decision on the rights of any transferee of the notes.[10] And the estate did not except to this limitation by the Court on the effect of its finding of constructive trust, even though the Court specifically provided an opportunity to any party to the proceedings to submit "objections and exceptions to the order at Alexandria, Virginia, at 9:00 o'clock a.m. on June 21st, 1971." The District Court, in its opinion from which this appeal is taken, addressed itself to the claim advanced by the estate that the earlier finding in May, 1971 bound Frost and Dreisen even though not then parties, and emphasized that, while describing the notes as "subject to pledge" thereby indicating that even the Court was unsure of the nature of the claim of Frost and Dreisen, it had carefully refrained in its May, 1971 opinion from making "any ruling concerning the rights of Frost and Dreisen, or the validity of any assignment of the notes in question." In the light of this record and the obvious purpose of the District Court, so definitely expressed, that in its May opinion, it did not intend to rule on the rights of Frost and Dreisen, but specifically reserved judgment on their rights, it would seem entirely improper to apply to Frost and Dreisen any mechanical rule of privity so as to bar them from a right to be heard on the existence *vel non* of a constructive trust in favor of the estate in and to the notes. After all, the principle of privity is not to be automatically applied in all cases as a basis for *res judicata*; its application for

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[10] It is not an unusual course for a court to follow in adjudicating issues that might prejudice parties who are not before the court to enter a provision saving the right of such parties. *See, Ladd v. Stevenson* (1889), 112 N.Y. 325, 19 N.E. 842, 844.

such purpose requires "careful examination into the circumstances of each case as it arises." *Storm v. Nationwide Mutual Insurance Company* (1957), 199 Va. 130, 97 S.E.2d 759, 762, 69 A.L.R.2d 849. On the basis of the "circumstances" of this case, the application of the principle, in our opinion, would not accord with fundamental fairness. The issue of a constructive trust in the notes in favor of the estate accordingly remains for resolution between the estate and the defendants Frost and Dreisen. The cause is remanded to the District Court to make appropriate findings on that issue on the record heretofore made before it, supplemented by any additional evidence either party may submit.

Though the case is being remanded for further proceedings, it is perhaps not amiss for us to note some additional points suggested by the parties in their arguments which we do not find dispositive of the cause as it is presently advanced. Thus, Frost and Dreisen suggested that the estate was foreclosed from maintaining any claim by a decree entered in a suit to quiet title to the Florida property filed by Do-Mor, in the state courts of Florida, and by a general release executed by Morrison in favor of Capital. Morrison was, it is true, a party to the suit to quiet title. That action, however, had nothing to do with the rights of Morrison to the notes given by Do-Mor to Capital. The issue in that suit to quiet title was Do-Mor's title, which rested upon a deed executed by Capital in favor of Do-Mor. No one in the action questioned Do-Mor's status of a purchaser in good faith for value without notice; and, under such circumstances, the general equitable principles stated in *Vicars v. Weisiger Clothing Co.* (1917), 121 Va. 679, 93 S.E. 580, 581, as quoted in the opinion of the District Court, which apply to transfers other than those qualifying as negotiable

instruments, sustained the claim of title of Do-Mor against any claim of Morrison. But Do-Mor's title to the real estate is entirely different from Frost's claim by virtue of an assignment after default to the notes in question. So far as the release is concerned—the other matter raised by Frost and Dreisen—it is the position of the estate that there was either a want or failure of consideration. While the District Court did not clearly rule on this contention of the estate, the fact that it did not predicate its conclusion on the release would suggest that it considered the position of the estate well-taken. The issue is, however, tied in to the question of a constructive trust and may be reviewed on remand on the basis of the evidence adduced on that issue.

Frost and Dreisen, also, have raised the issue of estoppel as against the estate. "It is essential," to quote the language of this Court in *Souter v. State Mutual Life Assurance Company* (4th Cir. 1960), 273 F.2d 921, 926, "that one invoking an estoppel shall have justifiably relied, to his detriment, on the conduct of the party sought to be estopped—that is, that he changed his position for the worse."[11] The only possible act of Morrison on which Frost could rely for an estoppel would be that, by conveying title to Capital, he put it in Capital's power to sell the property and take purchase-money notes in payment with its name as payee, thereby indicating that Capital or its successor corporate "shell"

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[11] To the same effect, *see, United States v. Fidelity and Casualty Co. of New York* (4th Cir. 1968), 402 F.2d 893, 898; *United States v. Glassman Construction Company* (4th Cir. 1968), 397 F.2d 8, 11; *Davenport v. Ralph N. Peters & Co.* (4th Cir. 1967), 386 F.2d 199, 207; *General Cigar Co. v. Lancaster Leaf Tobacco Co.* (D.C. Md. 1971), 323 F.Supp. 931, 939.

was both the nominal and the real owner of the notes.[12] To predicate an estoppel on any such circumstances in favor of one not a holder in due course would be to thwart the basic purpose of the Commercial Code and to nullify its specific provisions. As we have already pointed out, when Frost took the notes with knowledge that they were past due and in default, he took "nothing but the actual right and title" of his assignor and he took "subject" to any claim "based on * * * breach of trust or duty or any other reason" including a "constructive trust or other equity against the instrument or its proceeds" in favor of "any person" which, of course, would include Morrison. Frost was an experienced lawyer, practicing in the City of Washington. Whether lawyer or not, he is charged with knowledge of the law as it fixed his rights under his assignment. Since the law specifically denied

[12] This follows from the finding of the District Court:

> "But even if it has established that fact (i.e., that Capital gave no consideration for the transfer to it), it was his (i.e., Morrison's) improper conduct which permitted Frost and Dreisen to purchase the mortgage in question free of notice of any claim of Morrison."

The "improper conduct" to which the District Court adverted was that Morrison "took no action to put prospective purchasers on notice of any latent claim until he filed the suit in Florida in September, 1966, long after the assignment of the mortgage by Capital, Southgate and others."

It is to be noted that the District Court consistently refers to "the assignment of the mortgage" rather than to the transfer of the negotiable instruments, overlooking the well-settled rule that the mortgage follows the obligation it secures and derives its negotiability from that of the obligation secured. 55 Am. Juris. 2d, Section 1308, at 1052. That the mortgage follows the note it secures and derives negotiability, if any, from the note is the rule in Florida where the land under mortgage in this case was located, *see Daniels v. Katz* (Fla. App. 1970), 237 So. 2d 58, 60; *Meyers v. Bryce* (Fla. App. 1957), 97 So. 2d 488, 489.

him any right to assume, when he took his assignment that there were no "equities or other claims of rights against the instrument or its proceeds," there was no representation by Morrison's conduct on which Frost had any "justifiable" right to rely that Benn and his corporate "shells" held title to the notes free from any equities in favor of either Morrison or any other party.[13]

Even if this controversy were not controlled by the clear provisions of the Uniform Commercial Code, we are not certain that the decree below could be sustained. Frost's standing as a *bona fide* purchaser for value without notice is open to serious question. His relationship with Benn was not casual. It was conceded that Benn frequented Frost's office, received mail there, and apparently gave Frost's office as the address for at least one of his "shell" corporations. Indeed, the very notes involved in this litigation had Frost's offices listed as the address of the payee Capital. Frost testified that this holding out of his offices by Benn was not with his approval and he said, when he heard of it, he ordered Benn to discontinue. But Benn was doing more than merely frequenting at odd times Frost's office; he had business dealings with Frost. Frost acted as attorney on behalf of several corporations connected in some way with Benn, with his fee guaranteed by Benn individually.

[13] There is reference, both in the opinion and in the argument, to the efforts of Morrison to conceal his property from his wife. Whether he transferred his property to Benn under what the law will regard as a trust because of some scheme to deceive his wife may aid the wife in her assertion of interest in the property so transferred but it cannot avail Frost and Dreisen. Benn's ownership of the property would be equally under a constructive trust, whatever may have been Morrison's reason for creating such a trust, and any transfer of the notes by Benn, if made after maturity and default, would be equally subject to the constructive trust.

He explained, however, that, while Benn was to pay his fee, Benn was not his client; in fact, he went further and stated that conflicts of interest would have prevented him from representing Benn in the litigation. Yet, conflict of interest or not, his fee was paid by Benn in the form of a credit of $50,000 against the purchase price of the very notes in litigation. Normally, he who pays one's fee is his client. Moreover, Frost concedes that Benn's operations were "unethical," though he testified that he did not discover this until a few weeks after he had purchased the notes. And, for some largely unaccountable reason, Frost would not take an assignment of the notes in his own name because he did not wish his name associated with the notes. And he purchased the notes at a considerable discount, a fact which, of itself, would not impugn the good faith of the assignment, but is a fact that can properly be considered in connection with all the other facts in the case, including the unique form in which payment was made by Frost to Benn.[14] It must be borne in mind that the notes, in default as they were, carried "suspicion" on their face. It is of interest that the assignment to Frost's nominee came after the District

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[14] *See, City of New Port Richey v. Fidelity & Deposit Co.* (5th Cir. 1939), 105 F.2d 348, 353, 123 A.L.R. 1352.

Frost claims he gave Benn five cashier's checks payable to Southgate Associates (one of Benn's corporate *alter egos*) for $18,000 each, his personal check for $5,000, payable to Southgate Associates, and $5,000 in cash. The balance of the purchase price of the notes in question, secured as they were by property worth, by Frost's own appraisal, $200,000, was in the form of a $50,000 credit on an attorney's fee due Frost by Benn. All in all, it must not be forgotten, though, that for a long time after this transaction, Benn and/or his corporate *alter ego* was representing the notes as "under pledge" and, as late as 1971 the District Court was still uncertain whether the notes were "under pledge," as its opinion of May, 1971 demonstrates.

Court had begun its consideration of the ownership of the Florida property and after Morrison had given notice, by his motion for leave to file a counterclaim, of his claim to the property or its proceeds. We are by no means as certain as apparently the District Court was that Frost could, even under the normal rules applicable to non-negotiable instruments, have qualified as a bona fide purchaser for value without notice. This is, of course, aside from the real issues in the case, which turn on the proper application of the Uniform Commercial Code for resolution.

REVERSED AND
REMANDED WITH DIRECTIONS.

APPENDIX G

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

Civil Action No. 2968

CAPITAL INVESTORS CO.,

Plaintiff,

v.

ARTHUR R. MORRISON, et al.,

Defendants.

MEMORANDUM OPINION

By order of December 16, 1971, Norman B. Frost and Harry Dreisen were made parties to this proceeding. The basis of such action was the allegation of the Estate of Arthur R. Morrison that it was the beneficial owner of two certain mortgage notes made by Do-Mor, Incorporated, dated June 21, 1963, secured by a mortgage on real estate in Brevard County, Florida, in the possession of said Frost and Dreisen.

I

In May 1963, Capital Investors Company instituted this action to clear the title to certain real estate acquired by it from Arthur R. Morrison and wife. It was thereafter expanded to encompass numerous other issues. Additional parties were added from time to time. The suit has been before the United States Court of Appeals for the Fourth Circuit on three occasions.[1] Just when it

[1] 360 F.2d 462 (1966); 387 F.2d 591 (1967); 453 F.2d 1365 (1972).

appeared the end of this litigation was in sight, this new issue arose. Many of the facts have been stated and restated, but some background is necessary for an understanding of the issue now before the Court.

A

Arthur R. Morrison and his wife, Marian Morrison, had marital difficulties. They litigated many of the issues relating to their jointly and separately owned properties in this suit. They owned jointly a parcel of land in Rosslyn, Virginia, which has been the principal subject of much litigation. They also owned a parcel of land in Brevard County, Florida. Mr. Morrison succeeded in getting title solely in his name. In the findings of fact made by Judge Butzner on December 17, 1964, hereafter referred to, he pointed out their marital difficulties and said that Mr. Morrison had pursued "a determination to get the property in his own hands and at the same time put Mrs. Morrison in a position by which he could effectively bring pressure to bear upon her for his own reasons." In order to obtain $30,000.00 cash, Morrison entered into negotiations with Malcolm B. Devers, a Florida attorney named Rossetter, and a Florida real estate broker named Pruitt. Pursuant thereto, a loan was obtained from First National Bank. Thereafter, to obtain an additional $30,000.00, Morrison agreed to convey the property to Rossetter and Pruitt for $360,000.00, upon the purchasers agreeing to assume the $30,000.00 loan from the aforesaid Bank. Morrison refused to complete the transaction. On March 18, 1963, Morrison entered into a contract to convey the Rosslyn and Brevard County property to Capital Investors Company (Capital). By warranty deed of June 21, 1963, Capital conveyed the Florida property to Do-Mor, Inc.

On the same day Do-Mor executed a mortgage to secure Capital $400,000.00 evidenced by four notes of even date:–

(a) One for $25,000.00 - payable on demand.

(b) One for $50,000.00 - payable on or before 2 weeks from date.

(c) One for $100,000.00 - payable $50,000.00 on or before one year from date, and $50,000.00 on or before two years from date.

(d) One for $225,000.00 - payable on or before 60 days from date.

On July 18, 1963, Do-Mor filed an action in the Circuit Court of the Ninth Judicial Circuit in and for Brevard County against Malcolm B. Devers and others. Mr. and Mrs. Morrison were made parties defendant and served by publication. Mr. Morrison filed an affidavit concerning the facts, but did not answer. Mrs. Morrison filed an answer and a cross-claim against Devers and Mr. Morrison. She claimed a one-half interest in the property. On April 19, 1964, a final decree was entered in that suit in which the Court found that none of the defendants had any interest whatsoever in the property involved in this litigation.

The Court decreed, among other things, that–

(a) It had jurisdiction of the parties and the property;

(b) That Do-Mor was the owner in fee simple of the property;

(c) That First National Bank held a mortgage for $30,000.00 on the property which was due and payable immediately with interest from the

date of the note executed by Malcolm B. Devers, dated June 28, 1962, and said mortgage constitutes a lien on the property;

(d) That title was confirmed in Do-Mor as against the claims or interest of all defendants (which included by name Devers, Arthur R. Morrison and M. A. Morrison) and all parties having or claiming any interest in said property;

(e) The claims, titles, rights, interest of all defendants are forever cancelled, and any cloud on the title is removed;

(f) The defendants "have no authority, right, title, interest, claim or demand of any kind and nature against the land hereinabove described . . . or against plaintiff, Do-Mor, Inc. as the owner of said land. ."

(g) All the defendants . . . are hereby forever enjoined, restrained and debarred from asserting either at law or in equity any claim, right, title, interest or lien of any kind or nature in, to or against land hereinabove described.

The aforesaid decree of the Circuit Court of the Ninth Judicial Circuit in and for Brevard County was on March 2, 1966, affirmed by the District Court of Appeals of the State of Florida. Frost and Dreisen assert that this action was an adjudication of the rights now asserted by the Morrison Estate; that giving full faith and credit to this decree, as this Court must do, the Morrison Estate cannot now maintain this action.

B

By release dated August 6, 1963, Arthur R. Morrison released and forever discharged Capital from all suits, actions, debts, dues, sums of money, etc., specifically including the property in Brevard County, Florida, "in-

cluding any and all monies due or to become due from Do-Mor, Inc., a Florida coproration, James H. Pruitt and his wife and others responsible and liable for said moneys."[2]

On December 17, 1964, Judge John D. Butzner[3] stated his findings of facts and conclusions of law in this suit. He found that the deeds executed by Mr. and Mrs. Morrison on July 25th and 29th, 1963, conveying the Rosslyn property to Capital, were valid and binding,[4] and that "neither of these conveyances were procured by actionable fraud."[5] Further, he found that the amount due should be secured by a deed of trust, "in the sum of $500,000.00 for each beneficiary,"—Mr. and Mrs. Morrison. Further, that if any credits were to be allowed, they would "be determined in the accounting," and the Court would "confer with counsel about the accounting between all of these parties." The findings further pointed out that—

> The question of indebtedness arising out of the Florida property, which Mr. Echols has raised, will be looked into. *There should be either some particularization of pleadings or amendment of the pleadings.* (Underscoring added.)

By a decree of this Court of June 29, 1965, Judge Butzner held—

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[2] By an agreement of July 29, 1963, Arthur R. Morrison had agreed the total sum due by Capital for Rosslyn and Florida property was not to exceed $1,000,000.00. A lien was taken on the Rosslyn property for this sum.

[3] Judge Butzner was elevated to the United States Court of Appeals for the Fourth Circuit in 1967.

[4] See opinion in 360 F.2d 462, 465 (4th Cir. 1966).

[5] Finding of Judge Butzner December 7, 1964. F & D Exhibit 45, page 9.

(a) The assignment of May 18, 1963, from Arthur R. Morrison to Capital;

(b) The affidavit of Arthur R. Morrison dated June 10, 1963;

(c) The statement of Arthur R. Morrison dated May 15, 1963;

"as having no effect against the title to the Rosslyn property."

> NOTE: This left title to the Florida property in Do-Mor, with the mortgage notes in Peters & Company.

Nothing further appears to have been done in this suit relative to the Florida property until September 14, 1970. The Court had scheduled a conference with all counsel for the purpose of determining what issues remained unresolved in this suit. At that time the Morrison Estate asserted it had a claim for the return by Capital and Benn of lands in Brevard County, Florida, or the proceeds of sale from said lands.

C

On September 9, 1966, Arthur R. Morrison filed an action in the Circuit Court of the Ninth Judicial Circuit in Florida in and for Brevard County against Do-Mor, Capital, Benn, Peters & Company, Harry Dreisen and other, wherein he asserted, among other things, that—

> (a) On May 18, 1963, Morrison entered into a contract to sell to Capital the Brevard County property, and in return Capital agreed to execute and deliver note payable to Morrison for $1,100,000.00 within five years.
>
> (b) That pursuant to the agreement, Morrison executed and delivered a warranty deed.

(c) Capital executed and delivered to Morrison two notes, one for $1,000,000.00, and one for $100,000.00[6] that the note for $1,000,000.00 was thereafter cancelled and in its place 50 notes of $20,000.00 each delivered; that the $100,000.00 note was cancelled on the representation the title to the Rosslyn property had been cleared.

(d) Capital entered into the said contract for sale, warranty deeds, etc. . . "for the express purpose and intent of defrauding the plaintiff."

(e) That on June 21, 1963, Capital conveyed the property to Do-Mor—Do-Mor executed a mortgage to secure 4 notes, etc.

(f) That the $50,000.00 note was assigned, and discounted to a third party, and that the 4 notes "were then assigned on August 12, 1963, by Capital to Brevard Properties, Inc" . . . recorded in Public Records.

(g) Subsequently, Brevard assigned the notes to Southgate Associates, Inc., on September 28, 1964, recorded in the official records. On March 16, 1965, Southgate assigned same to Peters & Company recorded in Public Records. Subsequently, Peters assigned to Harry Dreisen on October 4, 1965.

(h) The above assignments were made without consideration and with knowledge they "were the result of a fraudulent and improper transfer of real property which is the subject of this litigation.

[6]It is agreed between all parties, and alleged by Morrison that the $100,000.00 note was to cover cost of removing the clouds from the title to the Rosslyn and Florida properties. Morrison testified in the record, Vol. II pages 205-206, that he agreed to sell the Rosslyn and Florida property for $1,100,000.00, with the $100,000.00 for use to clear the titles.

(i) That an injunction be issued prohibiting Do-Mor and Pruitts from paying any sums, until the Court makes a final adjudication—and that the Court impress a lien on the property.

An amended complaint was filed in said suit June 22, 1970. It was alleged—

(a) The agreement of July 23, 1963, concerned itself with only the Rosslyn property and was a substitution and novation of the May 18, 1963 agreement; that as a result thereof, Capital held the Brevard property as a resulting or constructive trustee for benefit of Morrison; that Capital had been engaged in the practice of fraud; that Morrison had a vendors lien on the property conveyed, etc.

(b) On October 20, 1970, plaintiff moved to add Frost as a party, which was denied.

(c) At a pretrial conference in December 1970, counsel for Morrison and for Harry Dreisen appeared, but no others. The pretrial order set forth that the parties admitted that on May 18, 1963, the parties entered into an agreement for the sale of the Brevard land. The sale, the giving of the mortgage, the assignment of the notes, etc., was admitted.

(d) On February 1, 1971, plaintiff moved for a continuance because plaintiff was unable to take the deposition of J.T. Benn. The motion was denied on February 12, 1971, and on that day a notice of dismissal was filed.

II

With the above background, we turn to the question of ownership of the notes made by Do-Mor and secured by the mortgage on the Brevard County property. The contention of the Morrison Estate has now resolved itself to the point of claiming ownership of the last two notes—one for $100,000.00 and one for $225,000.00—secured by the mortgage.

A

At time of conveyance of the Brevard County property on June 21, 1963, a mortgage securing $400,000.00 was executed. An additional $60,000.00 was paid or assumed. The first note of the mortgage of $25,000.00 was paid. The second note of $50,000.00 was sold or hypothecated to Marian Morrison. The last two notes were on August 10, 1963, assigned to Brevard Properties, a Florida Corporation. On or about September 28, 1964, Brevard assigned the note to Southgate Associates, Inc., a Delaware Corporation. On or about March 16, 1965, Southgate assigned the notes to Peters & Company, a corporation of the District of Columbia. Peters took the notes as nominee of Frost.

B

On or about February 20, 1965, James T. Benn, President of Southgate, contacted Norman Frost relative to discounting the two notes of Do-Mor of $100,000.00 and $225,000.00. Before purchasing the notes and assignment of the mortgage, Frost requested Rex Peters, a real estate broker of Washington, to visit the property in Florida and determine its value, future use, condition, etc. Frost reviewed the papers in the suit which had earlier been brought by Do-Mor to clear the title to the property, and reviewed a title policy insuring the title. Further, he talked on two occasions to a Mr. Royster[7] of Do-Mor by telephone, and advised him he was considering a purchase of the notes. He inquired concerning the value of the land and what, if anything, had been paid

[7]The transcript of the testimony is not available, and this name is taken from a memorandum kept by me. The name of this individual may not have been Royster.

on the notes. Frost was informed that no part of these notes had been paid; that the value of the land was so far below the amount owed, that Do-Mor had abandoned the property, and that the property had depreciated in value. From Peters' view of the property and information which he was able to obtain from talking to the President of Do-Mor and others, Peters felt $200,000.00 was a fair value. Benn had said the property was worth $175,000.00. Frost purchased said two notes on or about March 17, 1965, and paid $150,000.00 therefor. The sum of $100,000.00[8] was paid in cash and a debt due by Benn of $50,000.00 was cancelled. Title to the notes was taken in Peters & Company. Thereafter, on December 8, 1965, Frost sold a one-half interest in said notes to Harry Dreisen for $75,000.00, together with an option to take up the other half.

Frost was not familiar with this suit which had been instituted to remove the cloud from the title to the Rosslyn property. The action above referred to instituted by Morrison against Do-Mor in Brevard County, Florida, in 1966, had not then been filed. Frost was not made a party to those proceedings. Since the purchase Frost and Dreisen have paid the taxes and other assessments against the property in the amount of some $130,000.00

It is clear that Frost paid $150,000.00 for the notes and thereafter Dresisen purchased a one-half interest for $75,000.00. It is further clear that Frost had no knowledge of the various litigation in which Morrison was involved, except the suit brought by Do-Mor to remove the cloud from the Florida property. That is, he did not have

[8]The payment was evidenced by $5,000.00 cash, Frost's check for $5,000.00, and 5 cashier's checks of $18,000.00 each payable to Southgate.

knowledge of the various claims of Morrison and his difficulties with Devers, Benn, Capital and others. He purchased the notes for value, without any notice of any claim by Morrison or any other party. He conferred with the maker of the mortgage and notes, Do-Mor, viewed the property, and inspected the title insurance policy. A check of the title records in Brevard County, Florida, did not give him any notice of a claim by Morrison. In fact, if Frost had reviewed the papers in this suit in 1965, at the time he purchased the notes, he would not have learned Morrison claimed the notes in question or the proceeds thereof. At that time, no pleading had been filed claiming the Do-Mor property or notes. If he had read Judge Butzner's Findings of Facts dictated December 17, 1964, he would have learned that the Court related that "The question of indebtedness arising out of the Florida property, which Mr. Echols has raised, will be looked into." But further, he would have discovered the contracts between Morrison and Capital for the sale and transfer of the Rosslyn and Florida properties; that by agreement of July 29, 1963, Morrison had agreed the total sum due by Capital for said Rosslyn and Florida properties was not to exceed $1,000,000.00, and that a lien had been taken on the Rosslyn property for the $1,000,000.00. He would have further found that the agreement of July 29, 1963, was said to be "the final and entire agreement between them and they shall not be bound by any terms, conditions, provisions, statements or representations not contained herein," and that any parole agreement was null and void.

C

In late 1970 and early 1971, when all parties were given an opportunity to state any and all unresolved claims or matters in this suit, the Morrison Estate then

asserted a claim to the proceeds of the notes in question. Frost, Dreisen or Do-Mor were not then parties to this suit. Morrison was the only party to this suit which had or claimed any interest in the notes or the property. The Estate asserted it was entitled to have Capital and Benn return the lands in Brevard County or the proceeds from the sale of said lands. It also sought the return of numerous papers.

Since no opposition was offered to the contentions of the Morrison Estate, this Court in an opinion of May 4, 1971, held that Capital was before the Court "and purportedly has title to and possession of the said deed of trust[9] notes made by Do-Mor, Inc. above referred to as numbers three and four, subject to a pledge, it would appear this Court has the power to enjoin Capital from making any transfer or other disposition of said notes until the matter can be fully resolved." The Court further held that Morrison was entitled to have all of the property returned to him, or the proceeds therefrom, "subject to the right of any bona fide transferee." In the opinion the Court further pointed out that actions had been instituted in Florida to settle some of the disputes relative to the title, ownership and claims to the Florida property, but that the record was "not clear as to what was undertaken, or what has been done."[10]

In the opinion of May 4, 1971, the Court pointed out that "[S]ome of the parties concerned [with the Florida property] are not before the Court."

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[9]The reference should have been to mortgage notes.

[10]The records of the Florida suits—(a) Do-Mor to clear the title, and (b) Morrison to establish his right to the notes, were not before the Court.

Nowhere in the May 4th opinion did the Court make any ruling concerning the rights of Frost and Dreisen, or the validity of any assignment of the notes in question. Nor did the Court intend to make any such ruling. It pointed out that the notes were "subject to a pledge," and that Morrison's rights were "subject to the rights of any bona fide transferee."

III

The parties agree that the issue is, what interest, if any, the Estate of Arthur R. Morrison has in and to the notes made by Do-Mor.

A

Frost purchased the notes in question from Southgate on or about March 17, 1965, for a valuable consideration. At that time there was no action pending wherein Morrison asserted any claim of record against either the Florida property or the notes. Not until September 9, 1966, did Morrison assert a claim of record against the property in Florida which had been sold to Do-Mor, or against the notes. He did not diligently prosecute that action, and it was dismissed or non-suited February 12, 1971. In that suit filed September 9, 1966, he alleged Capital assigned the notes to Brevard on August 12, 1963; that Brevard assigned them to Southgate September 28, 1964; on March 16, 1965, Southgate assigned to Peters & Company; and Peters assigned to Dreisen October 4, 1965. It was alleged all of the said assignments were by instruments duly recorded in the public records. That is, all assignments were matters of public record.

Even though Morrison either knew or could have learned from examination of the public records, that Capital assigned the notes to Brevard August 1963, and

that Frost through Peters & Company, acquired the notes in March 1965, he took no action to acquire a reconveyance of the property or to impound or acquire the proceeds until he filed action in Florida in September 1966. Morrison knew that Capital and Benn were before the Court in this case and that Peters & Company had its principal place of business in Washington, D.C., yet it made no effort to present the matter to this Court until September 1970.

Morrison in his amended complaint filed June 22, 1970 in the Florida suit instituted by him alleged that Peters & Company was nominee for Frost and that the notes were payable at Frost's office in Washington. While an unsuccessful motion was made to add Frost as a party defendant to the Florida suit, no effort was ever made to institute action against Frost and Dreisen in Washington, D.C., where they had offices and where Frost lived.

If Morrison had desired to assert his claim to the Florida property, or the notes given for the purchase price, he could have done so in the action instituted by Do-Mor in Florida in July 1963 to remove the cloud from the title. He knew he had conveyed a fee simple title in the property to Capital in May 1963; that Capital had sold and conveyed it to Do-Mor on June 21, 1963; and that on July 18, 1963, Do-Mor filed an action to remove any cloud from the title and to establish absolute title and ownership in itself. He and Mrs. Morrison were named as parties to that suit. Mrs. Morrison appeared and answered. In that suit Devers asserted that Morrison had conveyed the property to him, and that he held a good title acquired prior to the conveyance made by Morrison to Capital. An affidavit was filed by James H. Pruitt, A.T. Rossetter, and the officers of Do-Mor alleging fee simple title had been conveyed by Morrison to Do-Mor

and that neither Morrison nor any other defendant "have any right, title, interest or claim against any of the property[11] described in said bill of complaint."

Marian A. Morrison asserted in said suit she was the equitable and beneficial owner of an undivided one-half interest in said property; that by means of coercion and undue influence of her husband with the connivance of Devers, she was persuaded to join the deed to convey to Devers. She also sought to contest a quitclaim deed to Do-Mor. However, she later withdrew all of her opposition.

B

Here we have a case where Frost and Dreisen are completely innocent of any wrongdoing. They paid a fair price for the assignment of the mortgage. They had no notice of any prior claim of Morrison. An examination of the record in Florida and conference with the mortgagor, Do-Mor, revealed no claim of Morrison or any equitable claim of any other person. An examination of the records in Brevard County revealed the proper assignments of the mortgage. If an examination had been made of the papers in this suit pending in Alexandria, it would not have revealed any equitable claim of Morrison. They acted in good faith and did all a prudent person would have been expected to do. Any interest which Morrison could have asserted had not at that time come to light. Morrison had not attempted to assert his claim in the Brevard County action brought by Do-Mor to clear the title. Not until quite some months after Frost and Dreisen acquired an assignment of the mortgage did Morrison

[11] The real estate and the mortgage were fully described in the complaint.

attempt to assert his claim. There was nothing of record to show Capital was not a bona fide holder, for value,[12] of the Do-Mor mortgage.

C

In 55 Am. Jur.2d; page 1049, §1303, subject Mortgages, it is stated that the general rule is—

> . . . one who has taken from the legal owner of a mortgage an instrument of assignment, or the delivery of evidentiary documents, in such manner as to convey the legal title to him, will prevail at law and in equity as against latent equities held by third persons, if he has taken the assignment in good faith and without notice, and has given such consideration for the assignment as creates an equity in his favor. In this respect it has been declared that although it is the duty of the assignee to inquire of the mortgagor, he is not required to inquire of the whole world as to latent equities.
>
> According to the view taken in some cases, protection is accorded a bona fide assignee of a mortgage even in cases where the mortgagee was not entitled to protection. Thus, where notes secured by a purchase-money mortgage are given a vendor in whose hands the land is bound by an outstanding equity, and such notes and mortgages are transferred to a bona fide purchaser, the latter has been held entitled to protection against the unknown equity.

[12] While Morrison asserts that nothing had been paid to him by Capital for the Brevard County property, an affidavit of J.T. Benn asserted that notes for $1,100,000.00 had been given for the purchase price of the Rosslyn property and the Brevard County property. This was what was called for by the contract. Affidavit and answer of Mrs. Morrison confirmed this. The agreement of July 23, 1963 between Morrison and Capital so provided.

In a note in 80 A.L.R., page 395, dealing with assignments of mortgages, the author says:

> . . . The principal difficulties of the subject concern the rights of the mortgage purchaser as against one having a latent equity either by reason of having taken an assignment of, or required some interest in, the same mortgage, or by reason of having some interest in the mortgaged property inconsistent with the claims of the mortgage purchaser.
>
> It should, therefore, be noted as a basis for a consideration of the decisions, that (in conformity to the maxim, "where the equities are equal, the law will prevail") it is a rule generally recognized that one who obtains the legal title with an equity—that is, in good faith, for value, and without notice—is entitled to prevail as against anyone holding a mere equity, whether the latter be prior or subsequent in time to his own. In other words, a purchaser for a valuable consideration without notice has an equity equal to that of any other claimant. See 10 R.C.L. (Equity) §135. Accordingly, it appears that one who has, in good faith, and without notice, taken from the legal owner of a mortgage an instrument of assignment, or the delivery of evidentiary documents, in such manner as to convey the legal title to him, will prevail at law and in equity as against latent equities held by third parties, if he has given such consideration for the assignment as creates an equity in his favor. DeWitt v. Van Sickel (1878) 29 N.J. Eq. 209; Tate v. Security Trust Co. (1902) 63 N.J. Eq. 559, 52 Atl. 313; GEORGE F. PERRY & SONS v. MAND (reported herewith— ante, 392; Dearman v. Trimmier (1887) 26 S.C. 506, 2 S.E. 501.

It seems clear that a purchaser, for value, of a mortgage or of property without notice of a latent equity,

takes free of the equity. *Vicars v. Weisiger Clothing Co.*, 121 Va. 679, 93 S.E. 580, 581; *Virginia Iron Co. v. Bond*, 111 Va. 319, 68 S.E. 1005; *Guss v. Sydney Realty Corp.*, 204 Va. 65, 129 S.E.2d 43, 49. In the *Vicars case, supra*, the Court, quoting from an earlier decision, said:

> In Snyder v. Grandstaff, 96 Va. 477, 31 S.E. 648, 79 Am.St.Rep. 863, Judge Cardwell says this:
>
> "A purchaser for value and without notice is not affected by any latent equity. A mutual mistake stands on the same footing as any other equity. Kerr on Fraud and Mistake, p. 436, specifically lays this down as to mistake: 'As against a bona fide purchaser for value without notice, no relief can be had in equity.' Almost the same words are used in Pomeroy on Equity, §776. But the case of Carter v. Allan, 21 Grat. 241, and on this point it is cited with approval in Rorer Iron Co. v. Trout, supra, is directly in point. 'The doctrine that the courts of equity will not grant relief against bona fide purchasers without notice has always been adhered to as an indispensable muniment of title. It is wholly immaterial of what nature the equity is, whether it is founded on a lien or encumbrance, or trust, or a fraud, or any other claim; for a bona fide purchaser of the estate for a valuable consideration without notice purges away the equity from the estate, in the hands of all persons who may derive title under it, with the exception of the original party whose conscience stands bound by the violation of his trust and meditated fraud.' In Rorer Iron Co. v. Trout, supra, the same broad doctrine is laid down: 'It cannot be questioned at this day that the purchaser for value without notice, actual or constructive, will not be affected by a latent equity, whether by lien, incumbrance, or trust, or fraud or any other claim.' "

The doctrine is reiterated in Rhea v. Shields, 103 Va. 312, 49 S.E. 70, and in Va. Iron Co. v. Bond, 111 Va. 319, 68 S.E. 1005, and cannot be controverted.

This is an action in equity. The equities are with Frost and Dreisen. Not only did Morrison know that Capital had sold the property to Do-Mor, and assigned the mortgage, but he took no action to put prospective purchasers on notice of any latent claim until he filed the suit in Florida in September 1966, long after the assignment of the mortgage by Capital, Southgate and others. He then permitted that suit to be dismissed. Not until 1970 did the Morrison Estate take any affirmative action in this suit to assert any such equitable claim. While the Morrison Estate contends the conveyance from Morrison to Capital was without consideration, it has not established that fact. But even if it has established that fact, it was his improper conduct which permitted Frost and Dreisen to purchase the mortgage in question free of notice of any claim of Morrison. Morrison has not come into court with clean hands. He was improperly attempting to prevent Mrs. Morrison from obtaining her share of the property. It was his conduct in this regard that prompted Judge Butzner on December 17, 1964, to state that Mr. Morrison had pursued for two years "a determination to get the property in his own hands and at the same time put Mrs. Morrison in a position by which he could effectively bring pressure to bear upon her for his own reasons." He now attempts to set up his misconduct and actions to regain property he conveyed away, and at the expense of innocent persons.

Too, Frost and Dreisen have advanced some $120,000.00 to maintain the property, for which the Morrison Estate says they are entitled to reimbursement.

The Morrison Estate has not carried its burden, and is not entitled to relief from Frost and Dreisen, the effect of which is to confirm the assignment and ownership of Frost and Dreisen to said notes of Do-Mor assigned to them as aforesaid. Counsel will within fifteen days present a properly endorsed order to carry out the findings of the Court, or in lieu of such an endorsed order, give notice of the time and place of presenting the proposed order to opposing counsel, serving with the notice a copy of the proposed order.

/s/ [Signature]
United States District Judge

Norfolk, Virginia

August 25, 1972

APPENDIX H

IN THE

UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF VIRGINIA

Alexandria Division

Civil Action No. 2968

CAPITAL INVESTORS CO.,

Plaintiff,

v.

ARTHUR R. MORRISON, et al.,

Respondents

OPINION AND ORDER

On motion of counsel for the Estate of Arthur R. Morrison, the Court issued an Order for Norman B. Frost and Harry Dreisen to show cause why they should not be made parties defendant to this action, to enable the Court to make a full determination of all matters in issue.

I.

Arthur R. Morrison owned property in Brevard County, Florida, of a value of about $400,000.00, and in Rosslyn, Virginia, of a value of about $1,000,000.00. Each parcel has been the subject of litigation. The issues in this action have, for the most part, centered around the Rosslyn tract, with other properties playing some part in the litigation. Each of the named parcels were the subject of contracts and dealings between Morrison, on the one hand, and Devers, Benn, Capital and others, on the

other hand. There has been much conflict in the evidence dealing with the Florida property, and considerable activity between the parties. The facts before the Court up to May, 1971, seem to establish that Morrison contracted to and did convey the property to Do-Mor, Incorporated, which executed a purchase money deed of trust. The notes secured by this trust are the subject of some of the issues here involved. Through various alleged assignments and transfers, it is asserted that two of the notes aggregating some $375,000.00 are now in the hands of Messrs. Frost and Dreisen. Morrison's Estate contends they have no legal title or interest in said notes, but that said notes are in fact its property.

In their motion to discharge and dismiss the rule to show cause why they should not be joined in this suit, Frost and Dreisen assert several grounds. The principal ground is that Morrison's Estate is estopped by the terms of a final decree entered in the Circuit Court of the Ninth Judicial Circuit in and for Brevard County, Florida, in a suit of Do-Mor, Inc., et als. against Devers, et als. They say that the final decree entered in that suit adjudged that Do-Mor, Inc. was the fee simple owner of said property and that the claims of all others persons "in and to the land—are forever cancelled." It is their contention this decree cut off and ended any claim which the Morrison Estate had to the notes in question. Nowhere in that decree is there mention of the aforesaid purchase money deed of trust, nor is there mention that that trust is not valid and subsisting. The Morrison Estate grounds its claim under that deed of trust. That suit was brought by Do-Mor to quiet its title. The issue of who was entitled to the sums secured by the deed of trust was not before the Court. Nor does it appear that Capital, James

T. Benn, Frost, Dreisen, or other wholly owned companies of James T. Benn were parties to the suit. Hence, there is grave doubt there could have been any adjudication of the validity of the trust, or the rights of anyone in and to the sums secured by that trust. The facts before the Court at this stage of the proceedings do not justify the Court in so holding.

II.

Frost and Dreisen say this Court is not the proper venue for determination of the issue in question, namely, the rights of the Morrison Estate in certain notes owned or formerly owned by Capital Investors and by it assigned. The notes are personal property, rather than real estate. Capital, Benn, and other interested parties are already before this Court. Venue to deal with the Florida real estate is not before this Court. But, the issue of the ownership or ownership interest in the notes is before the Court. All the necessary parties to the determination of that issue, except Frost and Dreisen, appear to be before the Court. If this Court lacks venue, it is difficult to understand what court could or would have venue. The parties reside in different states, many could not be served with process in some states, and other complications exist. It would seem this Court has ancillary venue: that is, since it had jurisdiction and venue of the principal issues and of the principal parties, it has jurisdiction and venue of the ancillary issues and parties. This is what Professor Wright referred to in "Wright on Federal Courts, 1963," page 17, where, in speaking on the subject, he said:

> By this concept it is held that a district court acquires jurisdiction of a case or controversy as an

entirety, and may, as an incident to disposition of a matter properly before it, possess jurisdiction to decide other matters raised by the case of which it could not take cognizance were they independently presented. Thus where the court has jurisdiction of the principal action, it may hear also any ancillary proceeding therein, regardless of the citizenship of the parties, the amount in controversy, or any other factor that would normally determine jurisdiction.

That there should be such an ancillary jurisdiction is, in some instances, virtually a matter of necessity. This is illustrated by the leading case of Freeman v. Howe.[1] In an action properly in federal court on the basis of diversity, Freeman, the United States marshal, seized under writs of attachment certain railroad cars. The mortgagees of the railroad then brought an action of replevin against Freeman in a state court, and had judgment there. On review of the state court decision, the Supreme Court held that a state court has no authority to interfere with property which is under control of the federal court. Such a holding is inevitable, if an unseemly conflict between courts is to be avoided and if the federal court is indeed to function as a court. But the mortgagees argued that to bar their action in state court would be to leave them remediless, since, as to them, there was no diversity and they could not proceed to assert their claim against the property in federal court. The Supreme Court said that this was a misapprehension. It said that any party whose interests are affected by the action in federal court in which that court has taken control of the property may assert his claim to the property in federal court, and that such a claim would be ancillary and dependent, supplementary merely to the original

[1] 1860, 24 How. 450, 16 L.Ed. 749.

suit out of which it had arisen, and maintained without reference to the citizenship or residence of the parties.

* * * * *

In addition to the cases in which property was under the control of the court, there was a group of cases holding that the federal court has jurisdiction to do those acts which it must do in order properly to effectuate its judgment on a matter as to which it has jurisdiction. Thus it may enjoin relitigation in state courts of issues already determined in a federal action, and issue such other writs as are needed to make its judgment effective. This jurisdiction, too, is required if the federal court is to make effective disposition of cases properly before it.

Again, in "Federal Practice and Procedure," Barron and Holtzoff, Rules Edition, Vol. 1, page 360, § 71, it is said:

As respects ancillary proceedings, the better rule would seem to be that if the main action satisfies the venue statutes, ancillary proceedings need not. In other words if the court has jurisdiction of the original action and the venue is proper or is not questioned, there need exist no independent grounds of jurisdiction over the ancillary proceeding nor can objections to the venue be entertained.

Under the circumstances, it would seem this Court is the proper venue to determine the issue. When the facts are more fully presented and the issues more clearly defined, it may well be the Court should not proceed to determine the issues.

III.

The Morrison Estate asserts that the rights of Capital and Benn in the aforesaid deed of trust have been determined; that Frost and Dreisen were the assignees or transferees of Capital and Benn; that the claim of Frost and Dreisen to the aforesaid notes secured by the deed of trust can rise no higher than Capital's or Benn's; that Frost and Dreisen are not bona fide purchasers of the notes, and hence are estopped to set up title to the notes. In the present state of the record, the Court declines to so hold.

IV.

It is therefore ORDERED that:

1. The motion of Frost and Dreisen to discharge and dismiss the rule to show cause why they should not be joined as persons needed for a just adjudication of the issues here is denied.

2. Norman B. Frost and Harry Dreisen are joined as parties to this proceeding and directed to file their response to the issues involved within twenty (20) days from receipt of a copy of this Order.

3. Upon said parties filing their response, the Clerk shall promptly advise the Court of this fact so that a schedule of procedure may be promptly set up.

4. Copy of this Order has this day been forwarded to counsel for the Morrison Estate and for Messrs. Frost and Dreisen.

/s/ [Signature]
United States District Judge

Norfolk, Virginia

December 16th, 1971.

APPENDIX I

IN THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
Alexandria Division

Civil Action No. 2968

CAPITAL INVESTORS CO.,
Plaintiff,

v.

ARTHUR R. MORRISON, et al.,
Defendants.

MEMORANDUM OPINION

This action has been pending since May 1963. It involves many issues and many parties. Five district judges have at various times presided and made rulings on issues presented to them. There have been two appeals to the United States Court of Appeals for the Fourth Circuit. 360 F.2d 462 (1966) and 387 F.2d 591 (1967). Following the affirmance in 1967 of rulings made, a further hearing was held by The Honorable John D. Butzner, Jr. on April 6, 1967. At that time rulings on numerous issues were made by Judge Butzner. Although no formal order has been entered to carry out those rulings, a transcript of the proceedings of that day clearly records them.

By order of August 25, 1970, all counsel were requested to file a brief statement of the undetermined issues in the case. Following a conference with all counsel held on September 14, 1970, an order was entered September 16, 1970, setting forth the issues remaining for disposition, and counsel were requested to

respond within 30 days (a) as to whether the issues remaining were clearly stated, and (b) to file memoranda setting forth detailed information on the issues in which they were interested, together with other information set forth in the order. Subsequently an order entered November 27, 1970, pointed out that counsel had not complied with the September 16th order and again directed counsel to comply therewith.

The order of November 27, 1970, pointed out that strict compliance with the September 16th order was required and permitted a filing of the memoranda called for thereby on or before December 31, 1970, and that no additional pleadings would be permitted after December 31, 1970. Counsel were also directed not later than January 31, 1971, to (a) complete discovery, (b) file a list of all unresolved issues asserted by their clients, with notice that a failure so to do would constitute a waiver thereof, (c) file a list of all witnesses intended to be called; and that not later than February 10, 1971, (a) all de bene esse depositions should be completed and (b) any and all exhibits filed with the Clerk. An ore tenus hearing was scheduled for March 1, 1970, at Alexandria, and counsel were advised the hearing would continue until completed. Counsel's attention was again called to the fact that strict compliance with the terms of that order was required.

On or about January 18, 1971, the Court prepared and sent to all counsel a memorandum compiled from the pleadings, briefly reviewing the proceedings, and again calling counsel's attention to some of the provisions of the prior orders, namely, that failure to comply with the terms of the Court's orders would constitute a waiver of the right to assert any claim theretofore asserted. The issues in the case were again set forth, with the assertions made by the parties in connection therewith.

The matter came on for hearing on March 1, 1971. Prior to that date information was presented that James T. Benn, who sought to assert claims in this suit, was involved in some criminal action in the District of Columbia, and because of some issue raised by him was, on or about January 4, 1971, committed to Saint Elizabeth's Hospital for evaluation. Bernard S. Cohen was appointed as guardian ad litem for him. Shortly before March 1, 1971, Mr. Cohen became ill, and his law partner or associate, Mr. Terrence A. Sidley, was appointed as a joint guardian ad litem for Mr. Benn. He was present throughout the proceedings of March 1, 1971. On March 1, 1971, Andrew Wood of the firm of Bremner, Byrne and Baber, counsel for Capital Investors Company (Capital), moved for a continuance on the grounds of the absence of James T. Benn, president of Capital. Terrence A. Sidley also moved for a continuance due to the absence of Mr. Cohen and Mr. Benn. A continuance was denied. Neither Benn nor Capital has listed any exhibits or witnesses as required by the prior orders of the Court. Because of the illness of Mr. Cohen, the Court granted Mr. Cohen and/or Mr. Sidley the right to file a memorandum within 30 days setting forth any claim or issue of Mr. Benn, or any prejudice to him by reason of a failure to continue the case. No such memorandum has yet been filed.

II.

Turning to the issues for determination, all counsel agree that they are the issues set forth in the memorandum of the Court of January 18, 1971. For quick reference, they will be listed as they appeared in the January 18th memorandum:

(A) Whether Arthur Morrison had endorsed to Mutual Aid, Inc., on or about January 30, 1967, one of the

alleged notes of $20,000.00 given by Capital Investors Company to Arthur R. Morrison as asserted by James T. Benn.

At the hearing on March 1, 1971, all persons present agree that the Court rule there is now no issue involved, and the Court holds it is not now an issue in this case.

(B) Whether there are 50 or 75 notes outstanding of $20,000.00 made by Capital, and if so, which are bona fide obligations.

Whether or not there are outstanding 50 notes of $20,000.00 each, made by Capital, as contended for by the Morrisons, or 75 notes as contended for by James T. Benn, and whether there is any contingent liability on Capital for more than 50 of said notes.

There were 50 notes of $20,000.00 each, made by Capital, originally issued. Upon assertion that 25 of the first series issued had been lost, 25 additional notes were issued. No request for payment of more than 50 notes has ever been made. No contention is made that more than $1,000,000.00 was ever due. The Court finds that there are only 50 notes of $20,000.00 which have any validity.

(C) Whether Benn acquired a claim from Marshall Diggs; whether the claim is valid, its nature, etc.

Any such claim, if it exists or ever existed, has not been properly asserted in this case and it is denied.

(D) What payments, if any, have been paid by Capital and/or Benn on the deed of trust held by Perpetual Building Association and/or Peoples Bank of Leesburg; the balance due under said deed of trust and to whom.

As to Capital, no such claim has been asserted, and therefore is denied. As to James T. Benn, no statement

of any such claim has been filed, nor have supporting documents been furnished to establish any such claim. The burden is on Benn to prove his claim. No witnesses have been listed, nor have any exhibits been filed. The claim is denied.

(E) Whether or not Morrison delivered any notes secured by the deed of trust of July 6, 1965, or any notes given to replace any of said originally secured notes, to Barclay Bank, Nassau, endorsed to Allied Creators, and whether said Company assigned any or all of said notes to John W. Karr, and whether either of said parties now have any interest or title to any of said notes or monies received by said trust.

No claim was asserted or proof offered to establish this claim, and the Court rules there is no issue here.

(F) Whether Benn has any claim against tenants Iorios, and whether it should be disposed of in this suit.

No claim having been properly asserted, and no proof having been offered relative to this claim, it is dismissed.

(G) The counterclaims of Marian A. Morrison against Capital and Benn for an accounting of sums received by them from certain prop- ty in Florida, and for funds due for sale of a note of $50,000.00 of $45,984.00 claimed to be evidenced by a check made by Do-Mor, Inc. upon which payment was alleged to have been stopped; together with costs and attorneys' fees.

On or about August 1, 1963, Marian Morrison delivered a cashier's check to James T. Benn in exchange for a promissory note dated June 21, 1963, in the principal sum of $50,000.00 made by Do-Mor, Inc. payable to order of Capital in two weeks, bearing interest at five per cent per annum. Benn also delivered to Mrs. Morrison a check of Do-Mor, Inc. payable to Capital,

dated August 1, 1963, in the sum of $45,984.00 Endorsements on both the note and check were made by Capital. When deposited for collection, payment of the check was refused. Capital, by endorsement of the check and note, became liable on each of said instruments. Hence, Marian Morrison is entitled to a judgment against Capital for $45,984.00, with interest at six per cent per annum from August 1, 1963, until paid.

Mrs. Morrison also contends she is entitled to a judgment for said sum against James T. Benn, upon his alleged personal promise to pay the debt. She calls attention to a letter dated August 1, 1963 [defendants' new Exhibit 1-MM, old Exhibit 66] which is a letter signed personally by James T. Benn, as support for such claim. However, nowhere in the letter is a promise to pay the debt. While Benn has not entered a plea of the Statute of Frauds,[1] we need not decide whether it may now be raised, as the evidence is not sufficiently clear to entitle Mrs. Morrison to a personal judgment against him.

(H) Claim of the Morrison Estate to require the return by Capital and/or Benn of lands in Brevard County, Florida, or the proceeds of sale of said lands; for return of copies of checks from Morrison to Malcolm B. Devers; assignment of Morrison's interest in Vadicos, and the Sunvale mortgage; the assignment of Morrison's claims against Stewart Ogilvie; together with miscellaneous papers given by Morrison to Capital and/or Benn.

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[1] Code of Virginia, 1950, as Amended, Section 11-2(4), which provides that no action shall be brought to charge a person upon a promise to answer for the debt or default of another, unless in writing. However, the statute may be waived. Ricks v. Sumler, 179 Va. 571, 19 S.E.2d 889. There are circumstances, however, when it need not be set out in the answer. Lawson v. States Const. Co., 193 Va. 513, 69 S.E.2d 450.

By a written agreement of May 18, 1963, Arthur B. Morrison agreed to sell and Capital agreed to buy certain real property and other assets located in Florida, as well as the Rosslyn property in Virginia, in exchange for a note of $1,100,000.00 payable within five years from date, bearing interest at 6%. By subsequent agreement between Mr. Morrison, Mrs. Morrison and Capital, it recited inability of Mr. Morrison to comply with the May 18, 1963 agreement, and provided Mrs. Morrison would join in a conveyance of the Rosslyn property in exchange for notes equalling $500,000.00. The agreement set forth that the total indebtedness of Capital "in connection with any and all transactions, agreements, contracts and other writings signed by Capital - - - shall not exceed the total obligation and indebtedness of one million dollars in notes, the cost of clearing the title should not exceed $100,000.00." The agreement further provided that said agreement of July 29, 1963 contained "the final and entire agreement between them and they shall not be bound by any terms, conditions, provisions, statements or representations not contained herein" and any parole agreement was null and void. The effect of the July 29, 1963 agreement was for Capital to acquire the Rosslyn property by issuance of notes for $500,000.00 to each of the Morrisons, subject to existing liens of $70,000.00, and to allow Capital $100,000.00 to clear the title thereto. This $1,100,000.00 was the total consideration for the contract of May 18, 1963. Hence, there was no consideration for the Florida property. The Florida real property had a valuation of at least $400,000.00. On or about June 21, 1963, Capital conveyed the Florida real property to Do-Mor, Inc. The principals of that company were A. T. Rossetter and James H. Pruitt. Mr. Morrison had previously dealt with these parties and had previously obtained a $60,000.00

loan on the Florida property from them, and had talked with them relative to a purchase. The purchase price for the Florida real property was $400,000.00, evidenced by four notes, number one for $25,000.00, payable on demand; number two for $50,000.00, payable July 1, 1963;[2] number three for $100,000.00 with $50,000.00 payable in one year and $50,000.00 payable in two years; and note number four for $225,000.00, payable in sixty days. Note number one was paid. Notes numbers two, three and four are unpaid. According to testimony of Benn, Capital transferred notes three and four to Brevard Properties, Incorporated, which transferred them to Southgate Associates, Incorporated, which corporations were wholly owned by Benn. In a Chapter X proceeding filed by Capital in Florida, it listed Southgate Associates, Incorporated, as a wholly owned subsidiary and listed the aforesaid two notes among its assets, subject to a pledge.

In the agreement of May 18, 1963, Capital agreed to make available to Morrison $25,000.00 within 30 days, $25,000.00 on June 1, 1964, and a like amount each year until clear title to the Rosslyn property was resolved. Default was made in such provision. The agreement referred to a schedule as attached, but no one has ever produced the schedule.

Actions were instituted in Florida to settle some of the disputes relative to the title, ownership and claims in and to the Florida property. The record is not clear as to what was undertaken, or what has been done. Some of the parties concerned are not before the Court. However, since Capital is before the Court and purportedly has title to and possession of the said deed of trust notes made by

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[2]This was the note sold to Marian Morrison mentioned in (G) above.

Do-Mor, Inc. above referred to as numbers three and four, subject to a pledge, it would appear this Court has the power to enjoin Capital from making any transfer or other disposition of said notes until the matter can be fully resolved.

It does not appear that Capital has in good faith undertaken to comply with its contract, or that it intended to fulfill its undertaking. It does not appear it has paid any consideration for the Florida properties. Capital took and held the assets described, transferred and conveyed as a constructive or resulting trustee. All of the properties were owned by Mr. Morrison. No consideration was paid by Capital. Mr. Morrison is entitled to have all of the property returned to him, or the proceeds therefrom, subject to the right of any bona fide transferee.

A constructive trust, or as it is frequently called, "an involuntary or implied trust, is a trust by operation of law which arises contrary to intention and in invitum, against one who, by fraud, actual or constructive, by duress or abuse of confidence, by commission of wrong, or by any form of unconscionable conduct, artifice, concealment, or questionable means, or who in any way against equity and good conscience, either has obtained or holds the legal right to property which he ought not, in equity and good conscience, hold and enjoy. It is raised by equity to satisfy the demands of justice." 54 Am. Jur. page 167, § 218, title TRUSTS. The author in § 219 continues:

> A constructive trust is substantially an appropriate remedy against unjust enrichment. It is raised by equity in respect of property which has been acquired by fraud, or where, although acquired originally without fraud, it is against equity that it should be retained by the person holding it. The availability of a constructive trust as a mode of relief against unjust enrichment is not, in general, affected by the fact that the plaintiff has a cause of action at law, as distinguished from equity, for damages or other relief.

And in § 220 on page 170, the author says the "forms and varieties of constructive trusts are practically without limit."

In § 193 [54 Am. Jur. page 152, subject TRUSTS] the author says:

> The doctrine of resulting trusts is a familiar one in equity jurisprudence. Most broadly speaking, a resulting trust arises from the nature or circumstances of consideration involved in a transaction whereby one person thereby becomes invested with a legal title but is obligated in equity to hold his legal title for the benefit of another, the intention of the former to hold in trust for the latter being implied or presumed as a matter of law, although no intention to create or hold in trust has been manifested, expressly or by inference, and although there is an absence of fraud or constructive fraud. Indeed, there is usually no element of fraud in a resulting trust, and the presence of fraud makes the trust a constructive one. The doctrine of resulting trusts is, as a general rule, operative in a proper case, whether the property involved is realty or personalty. Under the trust theory, the taker of the original title never had any beneficial interest, and once sufficient basic facts are established, equity will enforce or execute the trust against the person so holding, in invitum.

See also Michie's Jur. Vol. 19, subject Trusts and Trustees, page 75, paragraphs 23, 24 and 48. In the case of *Smith v. Smith*, 200 Va. 77, 104 S.E.2d 17, at page 20, the Court said:

"A resulting trust arises where a person makes or causes to be made a disposition of property under circumstances which raise an inference that he does not intend that the person taking or holding the property should have the beneficial interest therein and where the inference is not rebutted and the beneficial interest is otherwise effectively disposed of." Vol. 2, Restatement of the Law of Trusts, pages 1244, 1245.

In *Peal v. Luther*, 199 Va. 35, 97 S.E.2d 668, at 669, it was said:

> . . . A resulting trust is created where a party makes or causes to be made a transfer of property under circumstances from which it is inferred that he did not intend that the transferee should have the beneficial interest in the property. An express trust is created where it is established that there was an affirmative intention to create it. In other words, a resulting trust is based on a presumption or inference of law from the circumstances, while an express trust is based on proof of the declared intention of the trustor. Young v. Holland, 117 Va. 433, 84 S.E. 637; Woods v. Stull, 182 Va. 888, 30 S.E.2d 675; 19 Michie's Jur., Trusts and Trustees, § 5 et seq., p. 50 et seq.; 54 Am. Jur., Trusts, § 187, p. 146; 89 C.J.S., Trusts, § 11, p. 722; 2 Restatement of the Law of Trusts, § 404, p. 1246. See also, Kellow v. Bumgardner, 196 Va. 247, 83 S.E.2d 391.

See also New Amsterdam Casualty Company v. Waller, 301 F.2d 839, at 842 (4th Cir. 1962), where it is said:

> A constructive trust is merely a procedural device by which a court of equity may rectify certain wrongs. It is suggestive of a power which a court of equity may exercise in an appropriate case, but it is not a designation of the cause of action which

> justifies an exercise of the power. Professor Scott put it pithily when he said of a constructive trustee:
>
> "* * * He is not compelled to convey the property because he is a constructive trustee; it is because he can be compelled to convey it that he is a constructive trustee."

And again at 843:

> Constructive trusts most frequently arise because of actual fraud or mistake. Professor Scott reminds us, however, that fraud or mistake is not invariably an essential ingredient. There may be a constructive trust, though there has been no mistake and though the constructive trustee's conduct was not reprehensible. Words of condemnation may become appropriate only when the constructive trustee seeks to avoid his duty to surrender the property by which he is unjustly enriched to the detriment of another.

Capital and/or James T. Benn are not entitled to have or hold the properties, real or personal, described in the agreement of May 18, 1963, except the Rosslyn property. They must surrender and return to Mr. Morrison's Estate the properties or the proceeds from any such properties sold or transferred, namely:

(a) Notes made by Do-Mor, Inc. numbered three for $100,000.00, and numbered four for $225,000.00, hereinabove described—representing proceeds from sale of the Brevard County property in Florida.

(b) Assignment of $129,705.40 in the form of note and mortgage, pledged with the First National Bank of Washington, D.C., for debt of approximately $112,000.00; Sunvale Corporation, maker; Jackson Vaughn, Esquire, Attorney and Trustee for Arthur R. Morrison.

(c) Checks from Arthur R. Morrison showing various amounts loaned by Arthur R. Morrison to Malcolm B. Devers, including a promissory note of said Devers or his corporation, payable to Morrison, aggregating some $74,322.74 principal, with interest.

(d) Claim of Arthur R. Morrison against Stuart Ogilvie of some $15,700.00.

(e) Arthur R. Morrison's right, title and interest in 200,000 shares of the capital stock of Vadico Terminals, Incorporated.

(I) Claim of Devers of $1,000.00 for legal fees in June 1963.

Claim of Devers for management fees for the period in 1963.

No claim on behalf of Malcolm B. Devers has been asserted, nor has evidence been presented to establish any such claim, nor does the record establish that Devers is entitled to any such sum. Hence this claim is denied.

(J) Claims of Benn and Capital against Morrison totalling some $95,943.40.

Claim of Benn against Devers for some $129,322.72.

No such claims have been presented for consideration by either Capital or Benn, nor has evidence been offered to establish such claims. The claims are denied.

(K) Claim of Benn against Mr. and Mrs. Morrison for $500,000.00.

In a pleading filed herein James T. Benn asserts this claim belongs to Capital. Capital has not asserted any such a claim. Benn says the basis of such a claim arises from a contention that Marshall Diggs was the owner of a one-half interest in the Rosslyn property, hence

he is entitled to one-half of the notes aggregating $1,000,000.00. It has already been determined Diggs did not own a one-half interest in the Rosslyn property. Diggs assigned his right in any such a claim to Capital.

No proof of the claim has been offered, nor did anyone at the hearing on March 1, 1971, ask the Court to consider the claim. It is denied.

(L) Claim of Benn against Mrs. Morrison for $10,000.00.

In a pleading filed by Benn October 20, 1970, he says this is a claim of Capital. Capital has not asserted any such a claim. No proof of it has been offered. It is denied.

(M) The amount of rents paid to the Clerk of the Court and the disposition thereof.

(N) What sums have been paid as rents for the property of Capital, and their disposition; the amount of taxes due on the property; and the amount of interest which has accrued under the deed of trust of July 6, 1965; what sum has been paid and to whom, and the interest now due and to whom.

The sum of $54,050.00 was paid to the Clerk of this Court on account of rents from the Rosslyn property for the period February 21, 1964, to March 1, 1971, together with $17,026.25 by transfer of interpleader funds from the Circuit Court of Arlington County, Virginia, paid in by Sarris. From such sums the Clerk paid:

Treasurer of Arlington County, real estate taxes	$13,388.24
Perpetual Building Association, on first trust	1,980.00
Peoples Bank of Leesburg, on trust	1,050.00

Magruder Insurance, casualty insurance	427.09
Clerk, Circuit Court of Arlington, attorney's fee for interpleader Sarris	437.50
Marian A. Morrison, as reimbursement cost of recording deed of trust, Capital to Echols and Luttrell, Trustees	2,011.00
Marian A. Morrison, disbursement from July 10, 1967 pursuant to court order	23,892.21
Arthur R. Morrison, or his estate, same	23,892.21
Balance on hand	4,000.00
	71,078.25

The trustees under the deed of trust from Capital to M. Patton Echols and Ralph J. Luttrell, Trustees, dated June 4, 1965, recorded July 6, 1965, recorded in Deed Book 1590 at page 485, of the Clerk's Office of the Circuit Court of Arlington County, Virginia, have filed a report showing sale of the property at a price of $700,000.00, which has been confirmed by the Court. The trustees' account shows the balance due on the deed of trust notes as principal of $1,000,000.00, with interest at six per centum per annum from August 1, 1963, through March 8, 1971, of $1,456,000.00. From the proceeds of sale the trustees paid:

Delinquent taxes of	$ 31,561.27
Balance due Perpetual Building Association, first lien	21,642.75
Peoples Bank of Leesburg, balance on first lien	29,328.70

Cost of sale	27,157.32
Deposited with Clerk pursuant to court order (a)	4,476.00
Deposited with Clerk pursuant to court order (b)	40,000.00
Deposited with Clerk pursuant to order (c)	292,916.98
Paid to Marian A. Morrison to be credited on her 25 notes of $20,000.00 each	252,916.98
	$700,000.00

(a) Deposited with Clerk to be held pending a determination of whether Marian A. Morrison is entitled to same.

(b) Part of the proceeds from sale due on the notes held by Marian A. Morrison, held to answer any claim found to be owing by her in this suit.

(c) Proceeds of sale due to holder of the notes formerly issued to Arthur R. Morrison, held to determine to whom they should be paid, and any claims against said sum.

Vouchers showing disbursements of said funds by the trustees have been filed with the papers in this suit and audited by the Court. They clearly show proper disbursements of said funds.

(O) Claims of Marian A. Morrison (1) to one-half of the rental payments received by Devers from the property for the period June 2, 1962 to August 1, 1963; (2) for payments on the prior mortgages and other claims made from August 1, 1963 to July 1, 1965; and (3) payments to stop foreclosure.

It is agreed by all parties that the claim of Marian A. Morrison to one-half of the rental payments collected by Devers is owing to Mrs. Morrison. The record of the hearing before Judge Butzner on April 6, 1967, clearly shows that Mr. Devers was required to account for rents collected by him. At the hearing on March 1, 1971, it was again agreed that this sum of $5,708.00 was owing to Mrs. Morrison from Devers, but counsel for Devers contended he was entitled to an offset for a claim of Devers against Mrs. Morrison, hereafter dealt with. Hence, Marian A. Morrison is entitled to a judgment against Malcolm Devers for $5,708.00.

Marian Morrison also claims $4,823.28 for sums paid by her on the liens of Perpetual Building Association and the Peoples Bank at Leesburg, which constituted first liens on the Rosslyn property, to prevent those lienholders from proceeding with foreclosure. These items were allowed by Judge Butzner at his hearing on April 6, 1967. At the hearing on March 1, 1971, they were admitted to be due. This sum should be reimbursed to Marian A. Morrison from the proceeds of sale. The trustees have deposited with the Clerk the sum of $4,476.00 to apply to this claim. Any order entered in this cause will direct the Clerk to pay the said $4,476.00 to Marian A. Morrison to be credited on the claim of $4,823.28, and to pay the balance of said claim of $347.28 from any remaining sums deposited with the Clerk to cover rents on the Rosslyn property.

(P) Whether Devers should be given a credit for the payment made to Marian Morrison of $10,000.00 about June 29, 1962, against his obligation for rents received by him.

This very same issue was before Judge Butzner when he conducted a hearing in this matter on April 6, 1967.

There, as here, the matter had been scheduled for disposition. Counsel for Devers desired to present the testimony of Devers. He was not present. When Judge Butzner adjourned for luncheon recess, he directed Devers' counsel to have Devers present to testify at the afternoon session, or he said "I will just proceed on his testimony he has already given and I would like you gentlemen to mark down the pages in the transcript." Later, Judge Butzner gave counsel privilege of filing memoranda and setting forth the parts of the transcript they intended to rely on, as well as the right to file affidavits. It does not appear any such memoranda or affidavits were filed. If they were, counsel have not called them to my attention.

This same question was listed as an issue for hearing and determination at the hearing on March 1, 1971. By order duly entered, counsel were required to file statements of the facts upon which claims were based, to file lists of all witnesses who were to testify, list all exhibits, and references to any testimony in the record which would be used or relied upon. No witnesses or list of exhibits was filed on behalf of Devers. Witnesses were listed and exhibits filed on Mrs. Morrison's behalf, opposing the claim. Devers' counsel offered some exhibits at the hearing on March 1, 1971, which are in the files. Hence they were not filed as required by the orders of the Court; they were not received. The same applied to any testimony which Devers sought to offer. On the other hand, counsel for Mrs. Morrison timely filed their contentions, supported by exhibits and testimony in the record. The record will show that the Court several times directed counsel's attention to the requirements of its orders to timely file statements of their contentions and what exhibits and witnesses would be presented to support the claims. Since no attempt was made to timely

comply with the orders, Devers' right to present evidence was waived.

Not only is the claim here made by Devers not substantiated, but the evidence presented on behalf of Mrs. Morrison establishes there is no merit to the claim, and it is denied.

III.

OTHER RULINGS BY JUDGE BUTZNER

There are two additional matters to be disposed of:

1. A sum of $10,000.00 paid by Devers to Mrs. Morrison in June 1963.

2. Rent collected by Devers for the period August 1, 1963 through July 1, 1965, due to Capital.

At the hearing before Judge Butzner held April 6, 1967, each of these issues was presented for a decision and ruled on. While no formal order was thereafter presented to Judge Butzner and entered by him, the transcript, which is a part of the record, sets forth the ruling. In the hearing which I have conducted in this matter, it has been made clear that any matter decided or ruled on by Judge Butzner would be binding and would be enforced.

As to the claim of $10,000.00 said to be due by Marian A. Morrison to Devers for an advance or payment made in 1963, pursuant to agreement between the parties, Judge Butzner ruled that sum was due by Marian A. Morrison to Devers, to be credited against any sums owed by Devers.

Lastly, as to rents collected by Devers from the Rosslyn property for the period of August 1, 1963 to July 1, 1965, Judge Butzner held that such sums had been

collected by Devers as a trustee and that he must account therefor. An accounting of such was prepared and circulated. There is no dispute of the amounts. Devers collected $24,550.00 and was entitled to a credit for $8,562.00 expended, leaving a balance due of $15,988.00. The funds are due to Capital. Devers will be required to pay said funds into the registry of the Court.

It was pointed out by the United States Court of Appeals for the Fourth Circuit in *Capital Investors Co. v. Devers*, 360 F.2d 462, 467 (1966):

> It is true that Devers has remained in possession of the property pending this litigation, but Capital has filed a claim against him for all rents collected. This claim will be heard in the forthcoming accounting proceeding in the district court. If Capital retroactively gains the benefits of possession, we think it must either account for the rents or pay interest on the purchase money for the same period.

Since Marian Morrison must pay $10,000.00 to Devers, she will be directed to pay said funds into the registry of the Court—or as a matter of accounting, have any sums due her from funds in the registry of the Court charged with said $10,000.00—and Devers will be required to pay the balance of $5,988.00 to the Clerk.

IV.

Counsel for the Morrisons are requested to prepare a proper order to carry out the rulings hereinabove made, and to circulate it among all counsel for endorsement. If all counsel cannot agree on the terms of the order, then the Court will hear objections and exceptions to the order at Alexandria, Virginia, at 9:00 o'clock a.m. on June 21st, 1971. At that time the Court will hear and determine any other issues in this cause which are ripe

for determination in order to bring this case to a final conclusion. A disposition of the funds in the registry of the Court must be provided for, and application of Roscoe C. Barnes and others to intervene for purposes of enforcing their judgment against Arthur R. Morrison must be ruled on. It may be some determination will have to be made relative to costs, and the fixing of a bond for any proposed appeals.

/s/ [Signature]
United States District Judge

Norfolk, Virginia
May 4th, 1971.

Supreme Court, U. S.
FILED
MAR 8 1979
MICHAEL RODAK, JR., CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1978

No. 78-1207

NORMAN B. FROST, Deceased,
and
HARRY DREISEN,

Petitioners,

v.

EXECUTORS OF THE ESTATE OF ARTHUR R. MORRISON,

Respondents.

BRIEF IN OPPOSITION
TO A
PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

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March 14, 1979

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QUESTIONS PRESENTED

1. Was the judgment of the Court of Appeals so supported by its findings of actual fraud that the law of the case was not a necessary ground of decision (i.e. obiter dictum)?

2. If a due process issue is in fact presented here:

a. Is it constitutionally permissible to apply the doctrine of law of the case to nonparties,

1) who are in privity with the party to the judgment, and acquired their interest in the notes after maturity, after the District Court had stated it would inquire into the Morrison claims to them, and after the filing of the Morrison cross-claim.

2) had notice of the hearing at which the judgment, the effect of which they seek to avoid was given, and

3) in effect resisted being added as parties to that hearing on a motion to join them?

b. Is it constitutionally permissible in applying the doctrine of law of the case to require a District Court to have a rational basis for overturning its earlier judgment, affirmed on appeal, including new evidence justifying a change of position, even from parties added after the original judgment who were:

1) in privity with the party to the judgment, and acquired their interest in the notes after maturity, after the District Court had stated it would inquire into the Morrison claims to them and after the filing of the Morrison cross-claim.

2) had notice of the hearing at which the judgment, the effect of which they seek to avoid, was given, and

3) in effect resisted being added as parties to that hearing on a motion to join them?

STATEMENT OF THE CASE

In 1964, Arthur R. Morrison made a claim in the District Court that he was the beneficial owner of a constructive or resulting trust in two promissory notes in the total face amount of $325,000.00. The notes were made by Do-Mor, Inc., a Florida corporation, and were secured by a mortgage on lands in Brevard County, Florida. The lands had been conveyed by Morrison to what the Court of Appeals for the Fourth Circuit was later to call a "shell" corporation (Petitioners' Appendix, page 63a), wholly owned by one James T. Benn, in May, 1963. Benn sold them to Do-Mor the following month in return for purchase money notes in the amount of $400,000.00.[1]

The claim to the notes was asserted by Morrison in 1964, in the first stage of this proceeding, and the District Court stated in December of that year that it would inquire into that claim. A cross-claim asserting the claim was filed in February 1965. A month earlier Morrison had brought suit in Florida asserting the claim and asking the Florida court to enjoin Do-Mor to pay him the amounts due on its notes.

Morrison died in 1970, before any action was taken in either suit. In the fall of 1970, the District Court set the issue for hearing in March, 1971, and the Florida suit was dismissed.

After Morrison's death, his Executors (hereafter the Estate) discovered that Benn had caused the notes to be assigned to first one and then to another of his wholly owned corporations. The second of these corporations had assigned the notes to a nominee of Norman B. Frost in March of 1965, after maturity and after the Morrison cross-claim had been filed. Frost was a lawyer in Washington, D. C., who was very much acquainted with Benn. Frost later described Benn as a "business associate". He had also done considerable work, paid for by Benn,

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[1] Ownership of the remaining two notes in the face amount of $75,000.00 was not an issue in the proceeding below.

in a suit in which the United States District Court for the District of Columbia had found Benn guilty of fraud, and gross fraud at that. See the opinion in Sankin v. 5410 Connecticut Avenue Corporation, 281 F. Supp. 524 (D.C.D.C. 1968).

During the fall of 1970, the Estate tried to persuade Frost to join voluntarily as a party in the hearing scheduled for March, 1971, together with his own assignee, one Harry Dreisen. When this attempt failed, the Estate filed a motion to show cause why Frost and Driesen should not be joined as parties pursuant to Rule 19 of the Federal Rules of Civil Procedure. The District Court denied the motion with leave to renew it. Frost and Dreisen had notice of the motion and the hearing. (Pet. App. 85a)

In an opinion dated May 4, 1971, the District Court imposed a constructive trust on the Do-Mor notes and Brevard County lands in favor of the Estate against Capital/Benn on the basis of fraud. After reconsideration was denied, this judgment was affirmed on appeals by Capital and Benn in Capital Investors Co. v. Morrison, 453 Fed. 2d 1365 (CA 4 1972).

The Estate thereafter renewed its motion to show cause and, over their objection, the District Court joined Frost and Dreisen as parties in its order of December 16, 1971. The petitioners' statement that they were added as parties after the imposition of the constructive trust is literally correct. Petitioners, however, have preferred not to state that Frost and Dreisen knew of the hearing many weeks before it was held, chose not to join as parties, and later resisted being added as parties when they were, in fact, joined.

After a hearing in early 1972, the District Court ruled that it would not impose a constructive trust in favor of the Estate against Frost and Dreisen. At this hearing, the District Court apparently assumed that its ruling with respect to the constructive trust against Capital/Benn was correct; but it found that Frost and Dreisen had no responsibility for Benn and his doings. (Pet. App. 92a)

The Estate appealed this adverse ruling of the District Court, which was dated August 25, 1973. The Fourth Circuit reversed on the ground that the District Court had failed to apply the provisions of the Uniform Commercial Code which governed the rights of the parties. It ruled that Frost and Dreisen could have no greater right to the notes than their assignor, Benn.

The Estate had contended before the Fourth Circuit that the District Court's ruling that the Estate had a constructive trust in the notes was res judicata as to Frost and Dreisen as parties in privity with Benn, taking after maturity and after Morrison had asserted his claim in the proceeding. The Fourth Circuit conceded that the position of the Estate was supported by precedent. (Pet. App. 70a). The Court, however, thought as a matter of fairness that Frost and Dreisen should be heard again, a second time, on the issue of the constructive trust between Capital/Benn and the Estate. The Court did not, as the petitioner asserts, (Pet. page 4) hold that Frost and Dreisen were not in privity with their assignor. Such a statement would have been a legal absurdity. What the Court did was to decline to apply the legal consequences of the relationship of assignor and assignee as it existed. Having told the District Court that they doubted that Frost was an assignee in good faith on any basis and stated their reasons, (Pet. App. 75a-77a), the panel remanded the case to the District Court to determine if there was a constructive trust on the existing record "supplemented by any evidence either party may submit."

On remand, the District Court heard the parties in the fall of 1974. At that hearing, the Estate submitted additional documentary evidence in proof of Benn's fraud. The petitioners had nothing to add. The record before the District Court consisted only of documents, depositions and transcripts of evidence at a hearing before another and different District Court judge.

On remand, in an opinion dated February 3, 1975, the District Court said nothing about the Uniform Commercial

Code. It had been instructed by the Fourth Circuit that Frost and Dreisen had only Benn's rights. It thereupon, with no new evidence as to Benn's probity and good faith, reversed its earlier holding saying that there was not and had never been any evidence of Benn's bad faith presented to it. Having washed Benn and rehabilitated his character,[2] the District Court found that his assignees had taken the disputed notes free of a constructive trust.

The Estate naturally appealed from this ruling. On appeal, the Fourth Circuit at first affirmed. It then reversed on the Estate's petition for rehearing. It then, on a petition for rehearing by the petitioners, set the case down for reargument. Having heard the parties again, the Court of Appeals on September 29, 1978, issued its opinion reversing the District Court. It ruled the Executors of the Estate "now have a constructive or resulting trust in the Florida land and are entitled to an order requiring the Defendants to convey it to them."[3] Judge Widener, who had written the first opinion on this appeal, dissented.

In its opinion, the Court found "the evidence of Benn's fraud is compelling." (Pet. App. 5a). It stated that:

> "What Benn did amply supports the finding that he never intended that the Capital Investors' notes be paid; he diverted all of Capital Investors' assets and stripped it of all means of payment." (Pet. App. 5a).

The Court, indeed, referred to other indicia of Benn's fraud: that he misrepresented Florida law to avoid giving the security Morrison asked; that he had thereby prevailed on Morrison to

[2]Benn had, among other things, pleaded guilty to a charge of mail fraud in the District of Columbia in 1972.

[3]Frost and Dreisen had foreclosed on the mortgage securing the notes in 1973. The foreclosure was completed several months after Frost's death and title to the lands was taken in the name of his personal representative and Dreisen.

accept unsecured notes of a shell corporation; that of the $225,000.00 he received from the notes he paid Morrison nothing,[4]

It described Benn as "an accomplished fraud artist" and listed certain of his accomplishments:

> "Benn was an accomplished fraud artist. On a plea of quilty, he was convicted in 1971 in the United States District Court of the District of Columbia of fraud by mail. In 1963, the Tax Court found him guilty of tax fraud. T. C. Memo 1963-151. In its opinion, the Tax Court referred to a pattern of acquiring valuable properties largely on the basis of notes which were, or became, worthless and which Benn never intended paying. The kind of complicated schemes in which he engaged are illustrated in the opinion of Judge Jones in Sankin v. 5410 Connecticut Avenue Corporation, D.C.D.C. 281 F. Supp. 524 (1968), in the opinion of Judge Fulton in Walsh v. Continental Insurance Underwriters Inc., (S. D. of Fla. No. 63-576-Civ-CF, 1965) and in the opinion of Judge Hoffman in Freehill v. Benn (E. D. of Va., No. 3421, 1969). He had the capacity of persuading even sophisticated business people to place their trust in him. Though he was not a lawyer, he dealt in legalisms. He convinced Morrison that he was a 'legal genius' and a helping friend. What he did to Morrison, however, was in the pattern disclosed in the court cases." (Pet. App. 5a-6a)

In pointing to Benn's fraud in these reported cases, the Court of Appeals followed the law established in Wood v. U. S., 16 Pet. 342 (1842), that proof of intent to commit fraud may be established by evidence of fraudulent conduct in other instances.

[4]Morrison admitted receiving something around $4,000.00 from Benn. Benn claimed to have paid about $17,500.00 for Morrison's Virginia and Florida lands. But none of these amounts came from the proceeds of the notes in issue.

The Court then summed up by noting:

"When he stripped Capital Investors of its assets and devoted them to his own use without paying the Morrisons, he clearly established that his intention, from the beginning, was not to pay the Morrisons." (Pet. App. 6a)

The Fourth Circuit also pointed out again as it had in 1973 (484 Fed. 2d 1157, 1164, 1165) (Pet. App. 75a), that Benn was no stranger to Frost:

"Frost, about whom the district judge was concerned, was not entirely an innocent, unsuspecting victim of deception. Several reasons for this are catalogued in the opinion reported at 484 F. 2d 1157 at pages 1164 and 1165.[5]. Frost, now deceased, was a reputable lawyer in the District of Columbia, but he knew Benn. His firm represented some of Benn's associates in the *Sankin* case. Indeed, he paid Benn only $100,000 for the two notes, the remaining $50,000 of the price being a credit for legal fees due Frost's firm by Benn's associates, the payment of which Benn had guaranteed. From the factsin the *Sankin* case, Frost was bound to have known the kind of man Benn was." (Pet. App. ibid)

After saying all this, the Court stated:

"Under the circumstances, we think the district judge was required to adhere to his earlier findings and conclusions that a constructive or resulting trust did arise."

The comment was mild and ertainly reasonable. "Under the circumstances," or stated another way, given such powerful evidence of fraud and with no contrary evidence, the Court of Appeals was of the view that the District Court had erred and had no choice but to adhere to its earlier finding of fraud. Petitioners, nevertheless, present this language as raising grave questions of due process and constitutional law.

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5 For the reasons given by the Court of Appeals in this opinion, see Pet. App. 75a, 76a.

REASONS FOR DENYING THE WRIT

1. THE JUDGMENT OF THE COURT OF APPEALS DID NOT DEPEND ON THE LAW OF THE CASE.

There is no necessity for this Court to decide the due process issue in upholding the judgment of the Court of Appeals.

The decision by Judge Kellam in the District Court was made on a record consisting only of documents, depositions and transcripts of testimony at a hearing before another judge. The Court of Appeals was not even bound by the clearly erroneous rule. Munters Corp. v. Burgess Industries, 535 Fed. 2d 210 (C. A. 2, 1976); Dopp v. Franklin Bank, 461 Fed. 2d, 873 (C. A. 2, 1972). It was free to consider the evidence and to arrive at its own judgment thereon. It was, of course, free to make its own legal conclusions.

The opinion, as quoted above, clearly states that the Court of Appeals found the evidence of fraud on the part of Benn overwhelming. There was, moreover, nothing to establish Benn's good faith in his dealings with Morrison, no evidence of his probity, nothing to challenge the conclusion that he had been engaged in a scheme to steal Morrison's property from the outset. With such proof of fraud the conclusion that Benn took and held Morrison's property as a constructive trustee followed as a necessary conclusion and the Court of Appeals so held.

The reversal of the District Court's ruling by the Court of Appeals was justified on the record before it. The observations of the Court of Appeals as to the law of the case were consequently in the nature of obiter dicta and unnecessary to support its judgment. That being so, the case presents no issue of due process and Fifth Amendment rights.

2. IN THE CIRCUMSTANCES, THE APPLICATION OF THE LAW OF THE CASE RAISED NO CONSTITUTIONAL ISSUE

Assuming for the purpose of argument that the judgment of the Fourth Circuit depended on the application of the law of the case to the issues before it, its application raised no issue of due process or violation of Fifth Amendment rights to justify the granting of the requested writ of certiorari.

Rule 19 of the Court sets out in general terms the kind of questions and issues that justify the granting of a petition for certiorari. None of the provisions of the Rule is in point here. The ruling by the Fourth Circuit is, if anything, in line with the law laid down by this Court in a similar case. Lamb v. Cramer 285 US 217 (1932). The petitioners have referred to no conflict between the circuits in any decisions on the issue presented. The supposed issue is not something new with which this Court has never grappled before, *Lamb v. Cramer*, supra, and which demands consideration and settlement now.

As noted, the issue presented here would seem to have been dealt with and disposed of in *Lamb*, decided almost two generations ago. There Lamb was an attorney to whom a client had conveyed certain property while her creditors were seeking to impose their claims against it. Judgment was eventually given for the creditors, with the Court reserving judgment as to Lamb's rights as grantee. When the creditors sought to have Lamb held in contempt for refusing to turn over the disputed property to them, the District Court ruled in Lamb's favor, on his plea, apparently, that he had not been a party to the action between his grantor and the creditors. The Fifth Circuit reversed, saying Lamb was bound by the judgment in favor of the creditors as a matter of res judicata. This Court affirmed on the ground that Lamb was in privity with his grantor and the judgment which determined her rights was binding on him.

Justice Stone, in the opinion, showed no sign of having misgivings on due process grounds in holding Lamb bound by the judgment.

It would seem to the Estate that *Lamb* disposes of the petitioners' case. Like Lamb, they were in privity with their assignor and took only his rights, as the Fourth Circuit had held in its opinion in 1973. (Pet. App. 69a). It is true that the Fourth Circuit denied the Estate the effect of res judicata. But in holding the petitioners subject to the more limited effect of the law of the case the Circuit could not be said, in light of the decision in *Lamb*, to have denied them due process. The application of res judicata, which the decision in *Lamb*, would have justified, would have limited the rights of the petitioners far more than the application of the doctrine of the law of the case. And if res jusicata, could be applied to a non-party to the judgment in *Lamb*, without violating his constitutional rights, application of the law of the case to the petitioners was a fortiori permissible.

But if *Lamb* does not dispose of the petitioners' case, there is nevertheless no sound basis for the petitioners' assertion that they were denied due process by the Court of Appeals.

This Court, in a number of cases in recent years, has extended the effect of estoppel by judgment in the interest of what is called judicial economy. Blonder-Tongue Laboratories, Inc., v. University of Illinois Foundation, 402 U. S. 313, 329 (1971), Parklane Hosiery Co., v. Shore, 47 U. S. L. W. 4079 (January 9, 1979). In these cases, this Court has shown its disposition to prevent parties from relitigating what has already been settled. Here Frost and Dreisen chose not to take part in the 1971 hearing. Had the decision then been adverse to the estate, they would undoubtedly have taken shelter behind it. They had notice of, but stayed away from, that hearing. Can they by staying away from the proceeding at that time avoid the effect not only of res judicata and estoppel by judgment, but of the law of the case as well?

The answer seems plain. To say that an issue of due process is involved seems to stretch the concept of due process beyond any reasonable or recognized limit.

The fact is that it is difficult to formulate the petitioners' idea of what would constitute due process in their situation. They refer to Pennoyer v. Neff, 95 U. S. 714 (1878). But they show not even the most remote cousinship to *Pennoyer*. They were properly added as parties over their protest late in 1971. They were heard not once but twice on their rights. Nor is there any kinship between them and the objecting parties in Hansberry v. Lee, 311 U. S. 32 (1940), which they cite. The disputed judgment here was given against Benn. Frost was Benn's assignee, after maturity and after the filing of the Morrison cross-claim. Dreisen holds his half interest in the notes by assignment from Frost. By any known definition they were in privity with Benn, who was bound bythe judgment that there was a constructive trust, a judgment which was affirmed on appeal. Application of the law of the case in such circumstances was a minimal burden on the petitioners. And it was a minimal protection to the Estate, which was, as already noted, normally and properly entitled to the protection of res judicata.

The only definite suggestion of the petitioners as to how application of the law of the case denied them due process is in their footnote 8 on page 11 of the petition:

> "As recognized by the dissenting Circuit Judge, the application of 'law of the case' in the instant case 'shifts the burden from Morrison's Estate, to prove its case as the proponent, to the defendants Frost and Dreisen to prove incorrect previous fact findings in a case to which they were not parties.' " (Pet. App. 12a)

Their point is, apparently, that after the Estate carried its burden of proof and received judgment in 1971, affirmed on appeal, it should have had to bear that burden again against them. They take the view that the judgment, even after being upheld on appeal, should have been treated as a nulity in the same case and

on the same issue. They complain at being obliged to prove that the earlier judgment was wrong. It may be easy to understand their complaint but it can scarcely be "elevatd to a constitutional level", to use this Court's phrase in United States v. Augenblick, 393 U.S. 348, 355 (1969). Indeed, in United States v. Tehan 365 Fed. 2d 191 (C. A. 6 1966) cert. denied, 385 U. S. 1012, it was held that there was no denial of due process in shifting the burden of proof to a party defending a charge of having violated the Ohio Blue Sky Law and requiring him to prove that the securities he sold were exempted from the provisions of that statute. The second hearing in which the petitioners took part was certainly fair. No right was denied them. There was no violation of any express constitutional mandate. Petitioners point to no case holding that a shift of the burden of proof in a civil trial violates due process. The Estate knows of none. And to require parties seeking to reverse a judgment to prove error in the judgment seems a thoroughly reasonable procedure. A presumption that a court always errs surely runs counter to every principle of jurisprudence recognized in the courts and that would appear to be what the petitioners ask this Court to hold.

It may also be that the petitioners are asserting that they were indispensable parties to any resolution of the dispute between Benn and the Estate in 1971 and that the judgment was consequently invalid without them. But strictly speaking, the issue as to the constructive trust between Benn and the Estate could be resolved only on evidence of the dealings between Benn and Morrison and between Benn and Morrison's Estate after his death. The petitioners at the first hearing, in 1972, in which they took part, went to great lengths to disassociate themselves from Benn's dealings and asserted only their own individual rights, independent of Benn's. But if they are now saying that they were indispensable parties to the hearing in 1971, it is clear that they made no effort to join in the proceeding and make their case at that time. Had they sought to do so, they had a procedure

available under Rule 19 of the Federal Rules of Civil Procedure, and could have appealed their exclusion from the hearing, had the District Court, in fact, chosen to exclude them.

The petitioners can scarcely argue that the law of the case is inherently unconstitutional and by its nature denies due process to the parties to whom it applies. The doctrine is not a novelty of the law, unknown to the petitioners at the time of the remand and invented thereafter. As the Fourth Circuit carefully stated, the doctrine is discretionary at most. It correctly pointed out that the doctrine does not prevent the doing of justice. It spelled out the reasons why it did not view Frost as the victim of any injustice. The reference to the want of new evidence was a correct statement of a bsic element involved in determining whether to overturn a judgment which has become the law of the case. Moreover, it should be said that no one barred the petitioners from introducing evidence of Benn's good faith in dealing with Morrison at each of the hearings in which they took part. They did not produce such evidence because none existed. There was nothing available to impeach the correctness of the District Court's holding in 1971 that Benn had engaged in a scheme to get Morrison's property without paying him for it.

What Frost and Dreisen are asking this Court to hold is that a District Court is free to overturn its own judgment, affirmed on appeal, without any basis in the record to justify such a change. If that were so, the provisions in the Federal Rules dealing with judgments would be without meaning. The powers of a District Court to alter its judgment are carefully stated in Rules 59 and 60 of the Federal Rules of Civil Procedure. The position taken by the petitioners would allow a District Court to overturn its judgment without any rational basis if attacked collaterally, even by a party in privity with the party to the original judgment.

In fact the petitioners go beyond that. Their contention is that as parties in privity with Benn, they were denied due process unless the District Court could change its 1971 judgment at its

discretion and without regard to the fact that its judgment has been affirmed on appeal. That leads, obviously, to another question: If a District Court may disregard a decision affirming its judgment, why may it not disregard a decision on appeal which reverses its ruling? The result which the petitioners ask would be to make judicial anarchy and disorder an essential element of due process.

The truth is that the doctrine of the law of the case does no more than insure a modest element of stability in thejudicial process. Lincoln National Life Insurance Company v. Roosth 306 Fed. 2d 110, 113, 114 (C. A. 5 1962). It leaves courts free to correct their past errors when justice requires. It allows parties to present evidence toward that end. It normally and reasonably requires new facts to justify changing a judgment; but it permits a change without such evidence when the interest of justice requires.

Looked at from a distance, it would seem that the petitioners gambled in 1971 on a decision in favor of Benn. Having lost that gamble and having lost in their attempt to establish rights superior to Benn's they now claim as a matter of due process that they are entitled to have the District Court overturn its 1971 judgment, though affirmed on appeal, with nothing to justify such a change. Their plea is, in short, that arbitrary action by the District Court is an indispensable part of due process.

The position of the Estate would be the reverse of the petitioners. The Estate would say that to allow such arbitrary action by a District Court would be to deny due process and to destroy any trace of order in the judicial system.

For the reasons stated, the Executors ask that the petition for certiorari be denied.

Respectfully submitted,

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